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Supreme Court of the United States,

OCTOBER TERM, 1928.

No. 77.

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, JAMES K. SYMMERS, GRACE B. DRAKE and EVERETT L. BROWN, as Executors under the Last Will and Testament of Herbert W. Brown, Deceased,

Plaintiffs,

against

THE UNITED STATES OF AMERICA,

Defendant.

On Certificate from the Court of Claims.

BRIEF FOR PLAINTIFFS.

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A. The policies of insurance which were taxed in this case were the exclusive property of Mrs. Brown and the children, Elizabeth and Richard Brown. They were no part of Mr. Brown's estate.

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Plaintiffs,

AGAINST

THE UNITED STATES OF AMERICA,
Defendant.

On Certificate from the Court of Claims.

BRIEF FOR PLAINTIFFS.

The Questions Certified.

Two questions arising herein have been certified to this Court by the Court of Claims of the United States, pursuant to § 288 of the Judicial Code.

Both questions involve the constitutionality of the final clause of § 402 (f) of the Revenue Act of 1921 (42 Stat. 227), under which an Estate Tax of $9,146.76 was imposed upon $160,888.21 of life insurance forming no part of the decedent's estate but paid directly to surviving beneficiaries under policies taken out by the decedent upon his own life.

Question I certified raises the question whether this tax is direct and consequently in violation of Art. I, Sec. 2, Clause 3, of the Constitution.

Question II certified raises the question whether the measure of the tax, even if held to be an excise, is so arbitrary as to render it unconstitutional under the "due process" clause of the Fifth Amendment.

Similar if not identical questions were considered, but not decided, by this Court in the case of *Lewellyn* v. *Frick*, 268 U. S. 238, which arose under § 402(*f*) of the Revenue Act of 1918. The opinion of the Court, by Mr. Justice Holmes, pointed out that "there would be a very serious question to be answered" before either the beneficiaries of the insurance or the Executors of the decedent's estate could be made to pay the tax. In that case, however, it appeared that the policies had been taken out *before* the passage of the Act, and on this ground it was held that the Collector could not include the insurance as a part of the estate in determining the tax; that is, that the Act was not retroactive.

In the present case the policies were taken out *after* the Revenue Act of 1921 was enacted, and the decedent died while the same Act was still in effect.

It appears from the Certificate of the Court of Claims that a decision upon the questions certified "is deemed indispensable to a proper disposition of this cause now before it and a proper discharge of the court's duties herein" (R., 7).

These questions have been certified in the following forms (R., 7):

> "Question I. Whether the tax imposed by the final clause of section 402(*f*), Revenue Act of 1921, 42 Stat., 278, on life insurance policies payable in terms to beneficiaries 'other than the decedent or his estate' is a direct tax on property and void because not apportioned.
>
> Question II. Whether the $9,146.76 tax imposed bears such an unreasonable relation to the subject matter of the tax as to render it void."

It may be noted that the language used in § 402(*f*) of the Revenue Act of 1921 (42 Stat. 227) under which this case arises, has been repeated in the later Revenue Acts of 1924 (43 Stat. 253), 1926 (44 Stat. 9), and 1928 (Pub. No. 562—70th Congress).

Statement of the Case.

The Plaintiffs sue as Executors of Herbert W. Brown, deceased.

September 13, 1922, upon Mr. Brown's application, the New York Life Insurance Company issued three policies of insurance amounting to $200,000, by which the Insurance Company agreed, upon Mr. Brown's death, to pay that sum, $200,000, to his wife, the beneficiary named in the policies. Each policy contained a provision permitting the insured to change the beneficiary (R., 4).

September 29, 1922, Mr. Brown changed the beneficiary of one policy, in the sum of $100,000, from his wife to their two children, Elizabeth and Richard, in equal shares (R., 4).

April 10, 1924, Mr. Brown died a resident of Westchester County, New York (R., 4).

July 30, 1924, the Insurance Company paid the insurance and accrued dividends to the Committee and Guardian, respectively, of the named beneficiaries, as follows (R., 5):

To the widow, Mabel L. Brown..	$100,444.10
To the two children, Elizabeth and Richard	100,444.11
Total (R. 5).....	$200,888.21

Mr. Brown left a taxable estate of his own property, after all lawful deductions (R., 14) of		$424,673.36
But to this, under § 402(*f*), Revenue Act of 1921, the Commissioner of Internal Revenue added the insurance paid the widow and children	$200,888.21	
Less	40,000.00	
Exempted by § 402(*f*) (R., 14) Total		160,888.21
Making, upon the Commissioner's valuation, a total taxable estate of (R., 14)		$585,561.57

Upon this valuation the Estate Tax, at the rates fixed in § 401 of the Act, amounted to $21,633.69 (R., 6). This tax was paid by the Plaintiffs, Mr. Brown's Executors, but under protest as to $9,146.76 thereof, because the Estate Tax was increased by that amount by the taxation (as if it had been a part of Mr. Brown's estate) of $160,188.21 of insurance received by Mrs. Brown and the two children under the policies of which they were beneficiaries (R., 6).

Pursuant to this payment under protest, and in due course, the Plaintiffs brought this action to recover $9,146.76.

Determination and Incidence of the Tax.

The Revenue Act of 1921 (42 Stat. 227) was in effect from November 23, 1921 to June 2, 1924.

The Act, in § 401, imposes "a tax * * * upon the transfer of the net estate of every decedent dying after the passage of this Act", according to stated rates. Presumably it is only the *transfer* of the *property of the decedent* that is intended to be taxed, if this section may be considered apart from other Estate Tax provisions of the Act.

But § 402(*f*), read with § 403, includes in "the value of

the net estate", and hence taxes at the highest rates applicable to the estate, all life insurance in excess of $40,000 payable to surviving beneficiaries, on policies taken out by the insured decedent.

The Act requires the Executor to pay the tax upon such life insurance (§ 406); makes him personally liable for the payment (§ 407); and, if not paid, the tax is a lien both on the decedent's estate and on the insurance itself; the Government can subject the property to the payment of the tax; and the beneficiaries are also *personally liable* for its payment (§ 409).

Having paid the tax, the Executor becomes, under § 408 of the Act, "entitled to recover from such beneficiary such portion of the total tax paid as the proceeds, in excess of $40,000, of such policies bear to the net estate". It follows that, if the decedent dies leaving any taxable estate of his own property, the Executor cannot recover the entire tax paid in respect of the insurance, but only a part of it. The distribution of the tax burden between the estate of the decedent and beneficiaries of the insurance necessarily varies according to the amount of the insurance, the value of the decedent's estate of his own property, and the rates to which the estate, by its size, becomes subject. In the present case, the proceeds of the policies in excess of $40,000 are 27.4% of the "net estate"; hence the Plaintiffs, as Executors, are "entitled to recover" from Mrs. Brown and the two children 27.4% of the total tax of $21,633.69, or $5,927.16, instead of $9,146.76 paid on account of the insurance, leaving $3,219.13 to be borne by the Plaintiff Executors; that is, the Executors of the Estate must pay 35.17% of the tax on the insurance and the beneficiaries of the insurance must pay 64.83% of it, or $5,927.16. The amount recoverable may be expressed arithmetically as follows:

Recovery	Total Tax	Proceeds over $40,000	Net Estate
X	$21,633.69	$160,888.21 :	$585,561.57

The relevent parts of the Estate Tax provisions of the Revenue Act of 1921 (42 Stat. 227), referred to above, read as follows:

"Sec. 401. That in lieu of the tax imposed by Title IV of the Revenue Act of 1918, a *tax* equal to the sum of the following percentages of the value of the net estate (determined as provided in section 403) is *hereby imposed upon the transfer* of the *net* estate of every decedent dying after the passage of this Act, whether a resident or non-resident of the United States:

1 per centum of the amount of the net estate not in excess of $50,000; * * *

4 per centum of the amount by which the net estate exceeds $250,000 and does not exceed $450,000;

6 per centum of the amount by which the net estate exceeds $450,000 and does not exceed $750,000;

[*Here follow the graduated rates and amounts from $750,000 up to $10,000,000*]

Sec. 402. That the *value* of the *gross* estate of the decedent shall be determined by *including* the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated * * *

(f) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess, over $40,000, of the amount *receivable by all other beneficiaries* as insurance under policies taken out by the decedent upon his own life.

Sec. 403. That for the purpose of the tax the value of the *net* estate shall be determined * * *

[by *deducting* from the *gross* estate determined as provided in Sec. 402, certain amounts for debts, expenses, losses, charitable gifts, etc., and a specific exemption of $50,000.]

Sec. 406. * * * The executor shall pay the tax to the collector or deputy collector * * *

Sec. 408. * * * If any part of the gross estate consists of proceeds of policies of insurance upon the life of the decedent receivable by a beneficiary other than the executor, the executor shall be entitled to recover from such beneficiary such portion of the total tax paid as the proceeds, in excess of $40,000, of such policies bear to the net estate. If there is more than one such beneficiary the executor shall be entitled to recover from such beneficiaries in the same ratio.

Sec. 409. * * * (*b*) if insurance passes under a contract executed by the decedent in favor of a specific beneficiary, and if in either case the tax in respect thereto is not paid when due, then the transferee, trustee, or beneficiary shall be personally liable for such tax, and such property, to the extent of the decedent's interest therein at the time of such transfer or to the extent of such beneficiary's interest under such contract of insurance, shall be subject to a like lien equal to the amount of such tax." (Italics ours.)

The procedure and result may be summed up as follows:

(1) Determine "the value of the gross estate", *including* life insurance payable to third persons (§ 402);

(2) Determine "the value of the net estate" by deducting from "the value of the gross estate" the items exempted in § 403;

(3) Determine the Estate Tax by applying to "the value of the net estate" so found, the progressive rates fixed in § 401.

(4) The tax so determined must be paid by the Executor (§ 406);

(5) Having paid the tax, the Executor of the estate is "entitled to recover" a part of it from the beneficiary of the insurance (§ 408); and

(6) If the Executor of the estate fails to pay the tax, then the beneficiary of the insurance is personally liable for "the tax in respect thereto", and a lien in favor of the United States arises upon such insurance or its proceeds (§ 409).

So ultimately the estate must pay a tax upon the proceeds of insurance of which it does not receive a dollar and the beneficiary of the insurance must pay a tax upon the insurance measured partly by the value of an estate of which he may not receive a dollar. The tax upon the insurance is measured by the highest rate applicable to the estate, and the greater the estate, the greater the tax burden upon the beneficiary of the insurance, who may have no interest in the estate.

Contentions of the Parties.

The Certificate of the Court of Claims states the issues between the parties as follows (R. 7):

> "The contention of the plaintiffs is (1) that the tax imposed on proceeds of the insurance policies mentioned is a direct tax and unconstitutional, and (2) even if an excise tax the measure of it is so arbitrary as to violate the due process clause of the 5th Amendment.
>
> The defendant contends (1) that the final clause of Section 402(*f*) of the Act is constitutional and (2) that it is not a direct tax but an excise, the measure of which bears a reasonable relation to the subject matter of the tax."

In the court below the Government contended (1) that the tax imposed by § 402(*f*) was not a direct tax but an excise tax (within *Knowlton* v. *Moore*, 178 U. S. 41; *Greiner* v. *Lewellyn*, 258 U. S. 384, and cases therein cited) measured by the value of the decedent's net estate; (2) that it was

constitutional to include in the measure of the excise, *i. e.* "the value of the net estate", something that was not a part of the estate and not in itself taxable, on the theory that a tax may be measured by any standard Congress chooses to adopt even though it embraces something that is not itself taxable; and (3) that the method of collecting the tax either from the Executor (who received none of the insurance) or from the beneficiaries (who *may* receive none of the estate) had no effect on the validity of its imposition.

FIRST POINT: QUESTION I.

The tax of $9,146.76 imposed under Section 402(*f*) of the Revenue Act of 1921 is a direct tax, is not apportioned and is void: Question I should therefore be answered in the affirmative.

This proposition resolves itself as follows:

A. The policies of insurance which were taxed in this case were the exclusive property of Mrs. Brown and the children, Elizabeth and Richard Brown. They were no part of Mr. Brown's estate.

B. The tax imposed is a direct tax on property by virtue of its ownership and is void because not apportioned.

C. The tax of $9,146.76 is not an "excise" tax within any definition ever suggested by this Court.

A.

The policies of insurance which were taxed in this case were the exclusive property of Mrs. Brown and the children, Elizabeth and Richard Brown. They were no part of Mr. Brown's estate.

It appears from § 401 of the Act that the Estate Tax is intended to be imposed upon "the net estate of every decedent" subject to it; that is, that it is the *decedent's property* that is to be taxed under the provisions of the Act and not the property of any other person.

But the treatment of the proceeds of the insurance policies under succeeding provisions of the Act, particularly § 402(*f*), raises the question whether the insurance money was the property of the decedent, Mr. Brown, or property of Mrs. Brown and their children, the beneficiaries to whom the Insurance Company was bound to pay the proceeds of the policies.

In the submission of the Plaintiffs a policy of life insurance is property, just as any other contract or promise to pay money is property. For a consideration the New York Life Insurance Company had undertaken to pay $100,000 to Mrs. Brown and $100,000 to the Brown children upon receiving due proof of Mr. Brown's death. The promise of the Insurance Company created in the beneficiaries a vested interest in the policies which was property of the most certain and valuable nature.

It would not be disputed that a corporate bond is property by which a corporation agrees to pay $1,000 ninety-nine years from date. The fact that the maturity is in one instance fixed by the calendar and in the other by the death of a third party is entirely immaterial. Such a bond is

indisputably property and the owner of that property is the individual to whom the money is to be paid. It seems equally clear that a life insurance policy is property and that the owner of that property is the individual to whom the proceeds of the policy are to be paid.

These propositions lead inevitably to the conclusion that the tax complained of in this case is unconstitutional, and may be supported by numerous authorities. A comprehensive discussion of the entire subject appears in the opinion of Chief Justice Rugg in the case of *Tyler, Administratrix, v. Treasurer and Receiver General*, 226 Mass. 306 (1917). In that case the court held life insurance policies not to be taxable as gifts made or intended to take effect in possession or enjoyment at the death of the grantor. The court says, at page 307:

> "A policy of life insurance is a contract. It is commonly a tripartite agreement, to which the parties are the insured, the insurer and the beneficiary. A policy of life insurance is a contract for a consideration paid, usually in money, in one sum or at different times during the continuance of the risk, which involves the payment of money or other thing of value by the insurer to the family, kindred, representative or other designated beneficiary of the holder of the policy, conditioned upon the continuance or cessation of human life, or which involves a guaranty, assurance or pledge of an endowment or an annuity. *Commonwealth v. Wetherbee*, 105 Mass. 149, 160. See St. 1907, c. 576, § 66; *Curtis v. New York Life Ins. Co.*, 217 Mass. 47. The rules applicable to the interpretation and enforcement of policies of life insurance are those which govern contracts. *Davis v. New York Life Ins. Co.*, 212 Mass. 310. While speaking with technical accuracy, a beneficiary is not a party to a policy of life insurance and could not at common law maintain an action in his own behalf, yet he has an equitable interest in the policy and can maintain an action for his own benefit, in the name of the personal representatives of the insured, and by statute is enabled to bring an action in his own name. *Campbell*

v. *New England Mutual Life Ins. Co.*, 98 Mass. 381, 400; St. 1907, c. 576, § 73. The rights of the beneficiary are thus protected by the law and by the statute. The rights of the beneficiary attach at once upon becoming so designated by the terms of the contract. *Pingrey* v. *National Life Ins. Co.*, 144 Mass. 374. Where the beneficiary is the wife of the insured, her rights instantly vest upon a meritorious consideration. *Bailey* v. *Wood*, 202 Mass., 562. It has been said that, apart from any statutory provision, the designation of a beneficiary in a policy of life insurance is in the nature of an executory trust for his benefit of which he cannot be deprived without his consent. *Bayden* v. *Massachusetts Mutual Life Ins. Co.*, 153 Mass., 544, 546. Said Chief Justice Fuller in *Central Bank of Washington* v. *Hume*, 128 U. S., 195, at page 206: "It is indeed the general rule that a policy, and the money to become due under it, belong, the moment it is issued, to the person or persons named in it as the beneficiary or beneficiaries. * * * *Gould* v. *Emerson*, 99 Mass., 154; *Knickerbocker Life Ins. Co.* v. *Weitz*, 99 Mass., 157." The rights of the beneficiary are vested when the designation is made in accordance with the terms of the contract of insurance. They take complete effect as of that time. They do not wait for their efficacy upon the happening of a future event. They are in no wise modified or increased at the time of the death of the insured.

The contract of life insurance differs from most other contracts, in that it is not intended ordinarily for the benefit of the insured, but of some dependent. Its original and fundamental conception is a provision by small, periodical contributions to secure a benefit for the family. While this conception has been enlarged in some respects, and especially in its commercial aspects, still the basic elements continue and are found in all the cases at bar. The insured retains no ownership of that which has passed to the beneficiary under the contract. *A reserved right to change the beneficiary does not affect the essential nature of the rights of the beneficiary so long as they last.* Whatever the insured does in way of designation of a beneficiary takes effect forthwith. If his act rightly be describable as a gift, it is a present gift which, so far as concerns him, takes effect at once both

in possession and enjoyment by the beneficiary. *Attorney General* v. *Clark*, 222 Mass. 291. There is no fund in which he has an ownership which is the subject of his act in designating the beneficiary, as in *New England Trust Co.* vs. *Abbott*, 205 Mass., 279, and *State Street Trust Co.* vs. *Treasurer & Receiver General*, 209 Mass. 373. The insured has no title to the amount due on the policy. He does not and cannot make a gift of that. The right to that amount as an instant obligation does not spring into existence until after his death. Even then the money belongs to the insurer, who is charged with the duty by the contract to pay to the beneficiary. So far as the insured is a 'grantor', to use the word of the statute, the only thing which he grants or can grant is an interest in a contract. So far as he can make a 'gift', the only thing which he has to give is a right in a contract. By designating a beneficiary both the 'grant' and the 'gift', so far as either exist at all, take effect in enjoyment and possession at once. Such a relation does not by fair intendment come within the descriptive words of the statute as 'property * * * which shall pass * * * by gift * * * made or intended to take effect in possession or enjoyment after the death of the grantor'." (Italics ours.)

It is established by numerous decisions that whether insurance policies are made payable to the decedent's widow or to some other individual and not to the decedent's estate, neither the policies nor the proceeds thereof form any part of the decedent's estate. Thus in *Matter of Voorhees*, 200 App. Div. (N. Y.) 259, 262, the court said:

> "The proceeds of a life insurance policy, made payable to the assured or to his estate upon his death, comes into his estate at his death, and then becomes a part of his estate. As such it is transferred as a part of his estate under his will or the intestate laws of the State. Such transfer of the proceeds is taxable (*Matter of Knoedler*, 140 N. Y. 377.) But if such a policy is payable, and is paid, to some other beneficiary named its proceeds never come into his estate and are not taxable under the Transfer Tax Law (*Matter of Parsons*, 117 App. Div. 321.)"

In *Wagner* v. *Thieriot*, 203 App. Div. (N. Y.) 757, 762, affirmed in 236 N. Y. 588, the court said:

> "The law is well settled that where, as in the case at bar, insurance policies are made payable to the decedent's widow neither the policies nor the proceeds thereof form any part of the decedent's estate. (*Dom. Rel. Law*, § 52; *Greems* v. *Tourer*, 87 Misc. Rep. 644; [aff'd. 164 App. Div. 968] *Kattel* v. *Domeyer*, 175 N. Y. 205; *Matter of Thompson*, 184 *id.* 36.) • • •
>
> When a husband takes out a policy on his life for the benefit of his wife he is deemed to act as agent for his wife. The wife in such case acquires a vested interest in the policy which may be defeated by death or by a change in the beneficiary where the right to make such change is reserved in or provided for in the policy (*Whitehead* v. N. Y. *Life Insur. Co.*, 102 N. Y. 143). • • •
>
> "The policy forms no part of her husband's estate and her only rights therein grow out of the policy itself and any collateral or additional agreements, by laws or contracts which form a part thereof."

The Court's particular attention is invited to its decision in *Washington Central Bank* v. *Hume*, 128 U. S. 195, which involved the right of creditors of the insured to life insurance policies which were payable to the insured's wife and children. The case does not appear to have involved any question with reference to provisions in the policies for change of beneficiaries, but the language of Chief Justice Fuller writing for the Court is comprehensive and conclusive on the point here. The Court held that neither the insured's administrator nor his creditors could recover any part of the insurance or the premiums paid by the insured to keep his policy alive. The opinion reads in part (pp. 206, 209):

> "We think it cannot be doubted that in the instance of contracts of insurance with a wife or children, or both, upon their insurable interest in the life of the husband or father, the latter, while they are living, can exercise no power of disposition over the same without their consent nor has he any interest therein of which he can avail himself, nor upon his death have his per

sonal representatives or his creditors any interest in the proceeds of such contracts which belong to the beneficiaries to whom they are payable.

It is indeed the general rule that a *policy*, and the *money* to become due under it, *belong, the moment it is issued*, to the person or persons *named in it as the beneficiary or beneficiaries*, and that there is no power in the person procuring the insurance by any act of his, by deed or by will, to transfer to any other person the interest of the person named. Bliss on Life Insurance, 2d ed., p. 517; *Glanz* v. *Glockler*, 10 Appellate Court Illinois, 484, per McAllister, *J.*; *S. C.* 104 Illinois, 573; *Wilburn* v. *Wilburn*, 83 Indiana, 55; *Ricker* v. *Charter Oak Ins. Co.*, 27 Minnesota, 193; *Charter Oak Life Ins. Co.* v. *Brant*, 47 Missouri, 419; *Gould* v. *Emerson*, 99 Mass. 154; *Knickerbocker Life Ins. Co.* v. *Weitz*, 99 Mass. 157.

This must ordinarily be so when the contract is directly with the beneficiary; in respect to policies running to the person insured, but payable to another having a direct pecuniary interest in the life insured; and where the proceeds are made to inure by positive statutory provisions.

* * * * * *

But, even though Hume paid this money out of his own funds when insolvent, and if such payment were within the statute of Elizabeth, this would not give the creditors any interest in the *proceeds* of the policies, which *belonged to the beneficiaries* for the reasons already stated." (Italics ours.)

The decision of this Court in the *Washington Bank* case has been widely followed in the state courts and has resulted in a long line of decisions which definitely establish the following propositions:

1. From the moment a life insurance policy is issued the beneficiary has a vested interest in the policy and the proceeds thereof.

2. That the premiums paid by the insured form no part of the proceeds of the policies.

3. That the insured's estate has no interest in or control over the policies or their proceeds.

4. That the reservation of a right to change the beneficiary which is never exercised does not affect the vesting of the estate in the beneficiary.

5. That the exercise of a power reserved to change the beneficiary divests the interest of the first named beneficiary and creates in the second named beneficiary a vested interest in the policy which is not affected by the reservation of power further to change the beneficiary so long as that power is not exercised.

Neary v. *Metropolitan Life Insurance Co.*, 92 Conn. 488, 103 Atl. Rep. 661;

Lloyd v. *Royal Union Mutual Life Ins. Co.*, 245 Fed. 162;

Arnold v. *Empire Mut. Ann. & L. I. Co.*, 3 Ga. App. 685, 60 S. E. 470;

Indiana Natl. L. I. Co. v. *McGinnis*, 180 Ind. 9, 101 N. E. 289;

Filley v. *Illinois L. I. Co.*, 93 Kan. 193, 144 Pac. 237;

Townsend's Assignee v. *Townsend*, 127 Ky. 230, 105 S. W. 937;

Anderson v. *Broad St. Natl. Bank*, 90 N. J. Eq. 73, 105 Atl. 599;

Estate of Andrew Carnegie, 203 App. Div. (N. Y.) 91, aff'd 236 N. Y. 517;

Matter of Miller, 236 N. Y. 290;

Matter of Parson's Estate, 117 App. Div. (N. Y.) 321, 102 N. Y. Supp. 168;

In re Vorhees Estate, 200 App. Div. (N. Y.) 259, 193 N. Y. Supp. 168;

Brown's Appeal, 125 Pa. St. 303;

Entwistle v. *Travelers Ins. Co.*, 202 Pa. St. 141;

Elliott's Appeal, 50 Pa. 75;

Anderson's Estate, 85 Pa. 202;

Holden v. *Insurance Company*, 77 So. Carolina 299 (1907).

When Mr. Brown took out the policies of insurance in question, there was created in Mrs. Brown a vested estate in those policies and their proceeds. This estate was subject to the condition of possible divesting in the event that Mr. Brown should exercise the power which he had reserved to change the beneficiaries. So long as that power was not exercised Mrs. Brown's vested interest remained. Mr. Brown did not retain any rights of ownership in the policies or in their proceeds. The policies were never a part of Mr. Brown's estate; they belonged to the beneficiaries named, *i. e.*, Mrs. Brown and (after Mr. Brown had exercised his privilege to change the beneficiary of one policy) the two children.

In this connection it may be noted that the beneficiaries had the right to pay the premiums and thus prevent the policies from lapsing. (37 *Corpus Juris*, 418; *Garner* v. *Germania Life Ins. Co.*, 110 N. Y. 266.)

The Government stated in its brief in the court below that in view of the reservation in the policies of power in the insured to change the beneficiary "the beneficiary has no vested right or interest during the lifetime of the insured." We submit that this is obviously incorrect and that it overlooks the distinction between a conditional limitation on a vested estate and the conditional vesting of an estate. When Mr. Brown took out the insurance policies in question, the New York Life Insurance Company made an absolute promise to pay the face amount of the policies to the beneficiaries named, upon the happening of a contingency. Thereupon the beneficiaries received vested interests in the policies. The death of Mr. Brown merely fixed the time when the payment was to be made. By reason of the reservation of power to change the beneficiary Mr. Brown retained the right to divest the interest of the beneficiaries named and vest that interest in other individuals. The result of such an action on Mr. Brown's part was no more and no less than a *transfer of a vested interest* from one person to another.

A contract of insurance is in many respects similar to

a corporate bond. Would the Government say that the owner of a corporate bond has no vested right or interest therein until maturity?

The gift of an estate to A if X reaches the South Pole is a conditional gift and creates no vested estate in A. But the gift of an estate to A until X returns from the South Pole does create a vested estate in A subject to be divested or terminated upon the happening of a condition.

So when Mr. Brown took out the policies, property rights in the policies vested at once in Mrs. Brown subject to be divested in the event that Mr. Brown should exercise his reserved power to change the beneficiary.

It was contended by the Government in the court below that the taking out of a policy of insurance is a "quasi testamentary act". To state this proposition would seem to be sufficient to demonstrate its unsoundness. The issuance of a policy of insurance has none of the characteristics of the execution of a will. A will must operate by virtue of statute law and must meet the requirements of the statute or fail as a will. Obviously the insurance policies in question have none of the characteristics of a will. A will is ambulatory in character and speaks as of the date of death. An insurance policy is a contract which comes into existence and creates rights and liabilities from the date on which it is made. The insurance policies in question neither meet with the requirements of the New York Statutes governing wills, nor do they have any of the characteristics of a will, and we submit that the Government's contention is manifestly unsound.

Moreover, it will be observed that Mr. Brown could exercise no testimentary act over the policies or their proceeds. He could not change the beneficiary by his will in a manner which might be considered analogous to the exercise of a power of appointment; for the policies themselves prescribe [R. 15] that a change of beneficiary to be effective must be endorsed on the policy by the company at its home office and "unless so endorsed the change shall not take effect."

The Government argued in the court below that where the right to change the beneficiary is reserved to the insured in the policy, the beneficiary has no vested right or interest during the lifetime of the insured and in support of this proposition the Government cited the following cases: *Reid* v. *Durborow*, 272 Fed. 99; *In re Greenberg* 271 Fed. 258; *Barbour* v. *Equitable Life Assur. Soc.* 174 N. Y. App. Div. 759; 161 N. Y. S. 469, aff'd 225 N. Y. 675, 122 N. E. 876; *Hopkins* v. *Northwestern L. Ass. Co.*, 99 Fed. 199; *Eltonhead* v. *Travelers Ins. Co.*, 177 App. Div. (N. Y.) 170; 163 N. Y. Supp. 838; *Wagner* v. *Thierot*, 118 Misc. 511, 194 N. Y. Supp. 610, aff'd 197 N. Y. S. 560, aff'd 236 N. Y. 588, 142 N. E. 295. In support of the contention that where the right to change the beneficiary is reserved to the insured the beneficiary under such a policy has a mere expectancy and not a vested right or interest therein, the Government in the court below cited the following cases: *Mutual Ben. Life Ins. Co.* v. *Swett*, 222 Fed. 200; *Mutual Reserve Fund Life Ass'n.* v. *Cleveland Woolen Mills*, 82 Fed. 508; *Lamb* v. *Mutual Reserve*, 106 Fed. 637; *Hopkins* v. *Northwestern L. Ass. Co.* (C. C. A.), 99 Fed. 199, 202; *Re American Range & Foundry Co.*, 14 Fed. (2nd), 308, 311; *In re* Hogan, 194 Fed. 846; *Brown* v. *Home Life Ins. Co. of N. Y.* (D. C.), 3 Fed. (2nd) 661; *Allen* v. *Diamond*, 13 Fed. (2nd), 579, 580; *Slocum* v. *Met. L. Ins. Co.*, 245 Mass. 565, 139 N. E. 816; *Mut. Benefit Ins. Co.* v. *Clark* (Cal.), 254 P. 306; *Barnett* v. *N. Y. Mut. L. Ins. Co.*, 66 Ind. A. 280, 114 N. E. 232; *Bost* v. *Volunteer State L. Ins. Co.*, 114 S. C. 405, 103 S. E. 771; *Mager* v. *Illinois L. Ins. Co.*, 211 Ill. A. 285; *Quist* v. *Western, Etc. L. Ins. Co.*, 219 Mich. 406; 189 N. W. 49; *N. Y. Life Ins. Co.* v. *Daley*, 25 Cal. A. 376, 143 P. 1033; *O'Donnell* v. *Met. Life Ins. Co.*, 11 Del. Ch. 4, 95 A. 289; *Mutual Life Ins. Co.* v. *Tuyman*, 122 Ky. 513, 92 S. W. 335; *Crice* v. *Illinois Ins. Co.*, 122 Ky. 572, 92 S. W. 560; *Strauser* v. *Met. Life Ins. Co.* (N. Y. App. Div.), 223 N. Y. Supp. 16; *Dunn* v. *New Amsterdam Casualty Co.*, 121 N. Y. Supp. 686.

Without referring in detail to each case cited, it is sufficient to say that the question involved in the great majority of these cases was whether under the particular facts there presented the interest of the beneficiary had been divested by acts of the insured where he had reserved in the policy power to change the beneficiary. In some cases the court held that the insured had complied with the requirements stated in the policy and in other cases the court held that he had not.

In none of these cases did the court *decide* that the interest of the beneficiary in such a policy was contingent during the life of the insured. There are dicta in some of the cases supporting the Government's contention, but such dicta are entirely irrelevant to the decision in each case.

In each instance the court might well have said that the beneficiary had a vested right in the policy subject to be divested by appropriate acts of the insured in changing the beneficiary; and such a statement of the law would have been entirely consistent with the decision of the court.

For example in *Reed* v. *Durborow*, 272 Fed. 99, an insurance policy was taken out by Durborow in which his sister was designated the beneficiary. The right was reserved in the policy for the insured to change the beneficiary. Intending to exercise this right the insured wrote to the company informing it of his intention but failed to comply with the requirements of the policy prescribing the method of such change. It was held that the attempted change of beneficiary was ineffectual and that the sister of the insured was entitled to the proceeds of the policy.

An examination of the other cases cited by the Government in this connection shows a corresponding failure to support the propositions for which they are cited.

The Government also argued below that a policy of life insurance is comparable to and may be treated on the same basis as (1) a transfer in contemplation of death, or (2) a gift to take effect in possession or enjoyment at the death of

the donor. Such contentions indicate, we submit, a fundamental misapprehension of the nature of life insurance.

A life insurance policy can in no sense be considered a "gift in contemplation of death" as this expression is commonly used in statutes and cases, since, in the normal cause, a life insurance policy can only be secured by persons who are in good health and not in contemplation of death. Moreover it can hardly be said that every person who takes out a policy of life insurance on his own life is in "contemplation of death". Of course, the applicant for life insurance is aware of the fact that death is certain to occur, but this knowledge cannot be characterized as a "contemplation of death" in the sense that this phrase is used in statutes and cases.

A life insurance policy is not a gift to take effect at death since it is not a gift at all but an independent contract. Moreover it takes effect and creates rights and liabilities from the moment it is issued; it takes effect immediately.

The Government placed considerable reliance in the court below on the case of *Will of Allis*, 174 Wis. 527, in which it was held that insurance policies on the life of a decedent can constitutionally be subjected to an inheritance tax. That case has no application whatever to the case at bar, since an examination of the opinion discloses that it turned upon a peculiarity of the Wisconsin law with respect to insurance policies. In the course of its opinion the Court quoted from *Rawson* v. *Milwaukee Mutual Life Insurance Co.*, 115 Wis. 641, as follows:

> "*In Wisconsin however, there has existed from early times a principle of the law of life insurance which is unique and at variance with the law in most of the states.* This principle is that a person who insures his own life for the benefit of another and pays the premium thereon may (except a limitation by statute as to a married woman) dispose of the policy by will or any other manner not inconsistent with the terms of the policy, to the exclusion of the beneficiary named therein." (Italics ours.)

The fundamental object of life insurance is protection. A life insurance policy is a contract of indemnity by which the company indemnifies the beneficiary against loss by death. Life insurance is in no sense an accumulation of an estate by the assured.

The Government in its brief in the court below argued that life insurance is in the nature of savings investment, and endeavored to draw an analogy between the deposit of savings in a bank and the payment of premiums by a policy holder. The Government argued that taking out a life insurance policy was equivalent to the assignment by a depositor of his savings account to his wife to be hers on his death. There is no analogy whatever. In the case of an assignment of a savings account to become the property of the assignee at the death of the assignor no present estate passes. It is in truth a gift to take effect at death. In the case of a policy of life insurance the gift, if it can be considered a gift at all, is *in praesenti*. Upon the issuance of the policy the beneficiary acquires vested rights therein. The death of the insured merely fixes the time when the insurance company is to pay over the proceeds to the beneficiary. In the case of an assignment of a savings bank account the thing that is taxed on the death of the assignor is the amount of the deposit, i. e., the amount which the assignor had actually deposited in the bank, plus the interest thereon. In the case of life insurance the tax is not on the amount of the premiums paid plus any dividends thereon. It is on the full amount of the proceeds of the policy.

The savings feature of life insurance is purely incidental. The amount which the insured pays in premiums is a sum which he pays for protection, and its temporary accumulation is merely what he pays for the advantage of not being compelled in old age suddenly to pay enormous sums each year for the current year's protection cost. In short, he pays in advance for a part of that future protection if he happens to live to old age.

The so-called dividends paid or accrued by a life insurance company are necessary excess payments in order to furnish a factor of safety. The reserve set up by insurance companies is not a saving to the policy holders at all. It is the mathematical sum necessary to be held to enable the company year by year to pay its death losses.

And finally it will be seen that the fallacies of these theories and suggestions of the Government in the court below are apparent from a simple illustration. Suppose a man dies after paying one premium on a policy of $100,000 payable to his wife. The widow collects $100,000 of insurance. How can it be said that the insured "saved" or "accumulated" $100,000 during his lifetime? Or that the insured by taking out the policy transferred $100,000 to his wife, either in contemplation of death or to take effect at death?

Moreover, it is to be noted that the Government attemps in this instance to tax not the amount of premiums paid, not the cash surrender value of the policy, not any interest which the insured owned during his lifetime, but the full amount of the insurance paid by the company to the widow under a contract entered into which created vested rights in the beneficiary prior to the insured's death.

B.

The tax imposed is a direct tax on property by virtue of its ownership and is void because not apportioned.

The history of the adoption of the Constitution reveals that the grant of power to Congress to levy "direct" taxes was the subject of heated debate. The states fought vigorously against surrendering the great source of revenue offered by direct taxation and the adoption of the Constitution was secured only by the compromise indicated by the rule of apportionment. That a direct tax cannot be imposed

by the Federal Government except by apportionment is emphasized twice in the Constitution:

> "Representatives and *direct* taxes *shall be apportioned* among the several states • • •" (Constitution, Article I, par. 2.)
>
> "No capitation, or other *direct* tax shall be allowed unless in proportion to the census • • •" (Constitution, Article I, par. 9.)

The framers of the Constitution were sensitive to the distinction between "direct" and "indirect" taxation and the quoted portions of the Constitution were to them vital and significant.

In view of the numerous opinions of this court in which the subject of direct taxes has been exhaustively considered, we hesitate to indulge at this point in abstract theoretical or economic speculations as to what are "direct" or "indirect" taxes. As stated in the opinion of Mr. Justice Holmes in *New York Trust Co. v. Eisner*, 256 U. S. 345, at page 349:

> "Upon this point a page of history is worth a volume of logic."

The name by which a tax is described in the statute is, of course, immaterial. Its character must be determined by its incidence. *Eisner v. Macomber*, 252 U. S. 189, 206; *Hanson v. Ky. Distilleries Co.*, 255 U. S. 288, 292; *Child Labor Tax Case*, 259 U. S. 20, 36, *et seq.*; *Hill v. Wallace*, 259 U. S. 44, 66, 68.

> "Taxation is eminently practical, and is in fact brought to every man's door, and for the purpose of deciding upon its validity a tax should be regarded in its *actual, practical* results, rather than with reference to those theoretical or abstract ideas whose correctness is the subject of dispute and contradiction among those who are experts in the science of political economy." (Italics ours.) *Nicol v. Ames*, 173 U. S. 509, 516.

The express prohibition laid by the Constitution on the taxing power of Congress that no direct tax shall be laid

except by apportionment has been frequently enforced by this Court. This Court has condemned in many instances attempts to establish as "indirect", taxation which in its actual practical results as brought home to every man's door is a "direct" tax on him, by taking away a part of his accumulated wealth simply because he owns it.

In *Eisner* v. *Macomber*, 252 U. S. 189, the Court held a tax on stock dividends to be a direct tax requiring apportionment.

In *Dawson* v. *Ky. Distilleries Co.*, 255 U. S. 288, the Court held a tax on whiskey withdrawn from bond or exported in bond to be a direct tax.

In the famous *Pollock* case, 157 U. S. 429, Chief Justice Fuller remarked, at page 558:

> "* * * a tax upon property holders in respect of their estates whether real or personal or of the income yielded by such estates and the payment of which cannot be avoided are direct taxes."

In *Knowlton* v. *Moore*, 178 U. S. 41, *Flint* v. *Stone Tracy Co.* 220 U. S. 150 and *Brushaber* v. *Union Pacific*, 240 U. S. 19, this Court reiterated and emphasized the cardinal principle that any tax levied on personal property because of its ownership is a direct tax.

If the taxes condemned in the foregoing cases were direct taxes, much more is the tax complained of here a direct tax.

Indeed from the Statute itself it appears that the tax complained of is a direct tax on the insurance. Section 409 of the Act provides that

> "* * * if insurance passes under a contract executed by the decedent in favor of a specific beneficiary and if * * * *the tax in respect thereto* is not paid when due, then the transferee, trustee or beneficiary shall be personally liable for such tax and such property * * * to the extent of such beneficiary's interest under such contract of insurance shall be subject to a like lien equal to the amount of such tax." (Italics ours.)

The Court's particular attention is invited to the italicized words in the above excerpt from the Statute. It is noted that the tax is not a tax "in respect" to the estate of the decedent; it is a tax "in respect" to the insurance itself. This language is susceptible of only one construction, namely that the tax is a direct tax on the insurance.

From the moment the New York Life Insurance Company issued the insurance policies in this case the beneficial interests in those policies vested in the beneficiaries therein named. These interests were owned by the beneficiaries a moment before Mr. Brown died. The same ownership continued in the beneficiaries after Mr. Brown's death. No change of ownership took place by reason of his death. Neither the policies nor the proceeds were ever part of Mr. Brown's estate. They were owned by the beneficiaries. After Mr. Brown's death the Commissioner of Internal Revenue attempts to take 6% of these proceeds (less $40,000) from Mrs. Brown and her two children by virtue of § 402(f) of the Revenue Act of 1921. If this is not a direct tax, what is it? The tax is attempted to be imposed on the $160,888.21 of life insurance owned by Mrs. Brown and her two children simply because they own it. This is not a tax for any privilege exercise by Mrs. Brown or her children except the privilege of owning property.

If it is said that this is an excise or an indirect tax, it may as well be said that the Income Tax of 1894 was an excise or indirect tax because it taxed only the privilege of a landlord of receiving and collecting his rent or of a capitalist of collecting coupons or dividends. Suppose a 6% tax were imposed on an individual by reason of his receiving $100,000 as the redemption value of corporate bonds or by reason of his receiving the sum of $100,000 in payment of a promissory note at maturity. What else could that be but a direct tax?

How could a tax be more direct than to take away 6% or 25% of the capital value of the property owned? It is neither more nor less than a capital levy on accumulated wealth. It is a direct tax if ever there was a direct tax and we submit

that it must be apportioned as required by the Constitution or fall as invalid.

Mrs. Brown held the promise of the insurance company to pay her $100,000 when her husband should die. That was a promise which had a value. On its maturity the United States asserts the right to take by taxation 6% of it. If that is not a direct tax on property, what is it? Suppose Mrs. Brown had in 1923 sold her right in the policy for say $10,000 to A. In 1924 when A collected $100,000 he could obviously be taxed on the $90,000 profit because of the Sixteenth Amendment; but must he also pay a 6% tax on the original $10,000 or on the $100,000? What would that be save a direct tax?

The tax attempted to be levied here is just as direct as if a 6% tax had been levied on a similar amount which Mrs. Brown and her children might have received from maturing corporate bonds or from an insurance company on account of matured endowment policies taken out by them on their own lives. In this connection we may refer in passing to the well established rule that payments by life insurance companies to beneficiaries cannot be deemed "income" in any constitutional sense (*Eisner* v. *Macomber*, 252 U. S. 189, 206; *Towne* v. *Eisner*, 245 U. S. 418, 425; *Doyle* v. *Mitchell Bros. Co.*, 247 U. S. 179, 185; *Southern Pac. Co.* v. *Lowe*, 247 U. S. 330, 335; *U. S.* v. *Phellis*, 257 U. S. 156, 168; *Merchants' L. & T. Co.* v. *Smietanka*, 255 U. S. 509; *U. S.* v. *Supplee Biddle Co.*, 265 U. S. 189, 194-5), but even if deemed income [and hence taxable without apportionment, 16th Amendment; *Brushaber* v. *Union Pacific*, 240 U. S. 1, 18; *Stanton* v. *Baltic Mining Co.*, 240 U. S. 103, 112, 113], then life insurance proceeds are expressly *exempted* by statute from taxation as income, because the "Income Tax" provisions of the Revenue Act of 1921 expressly provide that the very comprehensive language defining gross income (42 Stat. 238),

> "*does not include* the following items, which shall be *exempt from taxation* under this title:

(1) The *proceeds of life insurance policies* paid upon the death of the insured.

(2) The amount received by the insured as a return of premiums or premiums paid by him under life insurance, endowment, or annuity contracts, either during the term or at the maturity of the term mentioned in the contract or upon surrender of the contract."

U. S. v. Supplee-Biddle Co., 265 U. S. 189, 195, is conclusive on this point.

There are today upwards of eighty seven billion dollars of outstanding life insurance in this country maturing at the rate of about one billion and a half each year. To secure the payment of those policies at maturity upwards of ten billions of assets have been accumulated. Those policies are property whether before or after the death of the insured, which event only fixes the maturity of the obligation. If Congress should levy a tax of 6% on the face amount of all policies held by all the policy holders of this country, the tax to be paid by the insurance companies out of the policies' reserves, could it be said that such a tax was an excise or indirect tax? Could it be said to be a tax for the privilege of holding insurance? Would it be other than a direct tax, pure and simple?

This Court has repeatedly held and stated that to levy a tax by reason of ownership of property is to tax the property, and we submit that to sustain the tax complained of here would be to open the door wide for the Congress to levy any and all kinds of direct taxes and avoid the condemnation of the prohibitions expressed in the Constitution by merely calling the taxes excise taxes.

In *Frick v. Llewellyn*, 298 Fed. 803, Mr. Justice Thompson, in a very able opinion, held that the provisions of the Revenue Act of 1918 (which correspond to the provisions of the 1921 Act under discussion in this case) imposing a tax on proceeds of insurance policies payable to beneficiaries other than the estate, were void as imposing a "direct" tax on

the beneficiaries' insurance without apportionment. A portion of the opinion reads:

> "If it be true that the policies in question, on the death of decedent, did not pass from decedent's estate by will, descent or distribution, and that no transfer of them was made in contemplation of death, within the meaning of the Act, they would not be subject to a tax imposed, either directly or indirectly, upon the transfer of the net estate of the decedent. Congress could impose a tax on such property, but not under the guise of an excise tax. The Supreme Court, in *Knowlton v. Moore*, 178 U. S. 41, 20 Sup. Ct. 747, 44 L. Ed. 969, and in other cases, has, with painstaking effort, pointed out, and elaborated with great clearness, the line of distinction which separates death duties, by whatever mode assessed, or by whatever name designated, whether probate duties, stamp duties, legacy taxes or estate taxes and those taxes which are imposed on property as such, because of its ownership and possession. The former may be exacted on the passing of property by will or descent as the result of death, as distinguished from a tax on the property itself. In other words, the estate duty is not on the interest to which some one succeeds on the death, but the interest which ceased by reason of the death. And so have legacy and inheritance taxes been sustained, not as a tax on the property itself, but upon its transmission. This because the right to take by devise or descent is a legal, and not a natural right, and the authority which confers it may impose conditions upon it. While the right to regulate successions is vested in the States alone, Congress has the power to levy taxes on the transmission or receipt of property, which is something apart from the right to regulate its transmission.
>
> The amount of the net estate here made taxable under the Act, was increased by the total amount of the policies involved; with the result that the amount of the tax in dispute was imposed upon, and arose solely from, the value of those policies included as a part of decedent's net estate. We must, therefore, inquire on what theory were they so included as a part of the estate. Insurance policies are property. Their legal status has been well

established by numerous authorities. In the case of *Tyler, Administratrix* v. *Treasurer and Receiver General*, 226 Mass. 306, 115 N. E. 300, L. R. A. 1917, D. 633, the Supreme Judicial Court of Massachusetts, in considering the question of the right to impose a tax on money paid to the beneficiary under an insurance policy, considered exhaustively, and laid down with clearness, the scope and character of insurance policies and the rights of beneficiaries thereunder. In substance, the Court held that a policy of insurance is a contract and that the rules which are applicable to contracts govern their interpretation and enforcement; that the rights of the beneficiary attach at once, when designated as such in the policy, and are protected both by common law and statute; that where the beneficiary is the wife, her rights instantly vest upon a meritorious consideration; that it is the general rule that a policy and the money to become due under it, the moment it is issued accrue to the person mentioned as beneficiary, that when the designation is made, his right is vested, taking complete effect as of that time, being in no wise modified or increased at the time of the death of the insured; that such contracts are usually for the benefit of some dependent, and the insured retains no ownership of that which has passed to his beneficiary under the contract, and that so long as they last the nature of the beneficiary's rights is not affected by a right reserved to change the beneficiary. If his designation be considered a gift, it is a present one, taking immediate effect, both in possession and enjoyment by the beneficiary. To the amount due on the policy, the insured has no title, the right to such amount does not spring into existence until after his death and even then, the money belongs to the insurer, who is charged with the duty under the contract, to pay to the beneficiary.

* * * * *

* * * *And finally, I am of opinion that in the three policies in which the assured reserved a right to revoke the assignments to his wife and daughter, but never did so, the rights of the assignees were vested and absolute; that those rights vested immediately under the assignment subject to a limitation; not a conditional estate, vesting at the time of death, but an estate which vested at once,*

subject to be divested by the happening of an uncertain future event. As that event did not occur, there was no divestiture.

Under these facts, the policies *being the property of others than the decedent*, upon what legal basis does the imposition of these taxes rest? It is defendant's contention that the property itself is not taxed; that the tax is an excise on the right to transmit property at death; that the inclusion of non taxable property in the measure of the tax, does not make the Act unconstitutional, if the measure of the excise be reasonable; and that it is reasonable to measure such tax by including the value of any property of which the decedent has made testamentary disposition; that the purchase of a policy of insurance on one's life is a testamentary disposition and therefore the Act is valid. The answer to this position is, that the Act undertakes to impose the tax upon the transfer of the net estate of the decedent, an excise on its passing as the result of death, as distinguished from a tax on the property itself. Here, there is no transfer at death, no passing of the property, upon whose value the percentages of taxation are based. Neither can it be said, as contended by the defendant in its supplemental brief, that if the taxes imposed by Sections 401 and 402(f) cease to be an estate tax by reason of the effect of Sections 408 and 409, it is transferred, not into a direct tax but into an excise on the right of the beneficiaries to receive the insurance. This because estate taxes and what are known as legacy or inheritance taxes, are of the same character, death being the source from which the taxing power arises.

Estate excise taxes are based on the power to transmit or the transmission from the dead to the living; while legacy or inheritance taxes are based on the transmissions or the right to receive the property in question. Here, the right of the beneficiaries to receive the insurance did not spring from the death of the testator. Their rights arose under contracts of insurance. The date of death is simply the time when the insurers become obligated to pay, and the beneficiaries entitled to receive, the proceeds of the policies under their contract. What Congress did under Section 402(f) was to impose a tax upon property, not an excise tax upon the happening of

an event. In *Pollock* v. *Farmers Loan & Trust Co.*, 158 U. S. 601, 15 Sup. Ct. 912, 39 L. Ed. 1108, the tax upon income derived from real estate and from personal property was held to be in effect a tax upon real and personal property. Here, the statute arbitrarily makes something a part of the Frick Estate which in fact was no part of it, and upon the value of that, undertakes to levy an estate tax, an *ad valorem* transfer excise tax, amounting to 25 per cent. of the value. This, in my judgment, is the taking of property without due process of law; the levying of a direct tax without apportionment as required by the Constitution.

It is difficult to understand on what hypothesis this tax can be held valid. It would appear to be an attempt to impose a tax on the amounts received by the beneficiaries under the policies, and to compel the executors to become the collectors of the tax, although such amounts constituted no part of the estate and were not received by, nor in any manner under the control of the executors."

On appeal in *Lewellyn* v. *Frick*, 268 U. S. 238, this Court affirmed the judgment below, but upon another ground, and did not pass upon the constitutional question, saying, at page 251:

"We do not propose to discuss the limits of the powers of Congress in cases like the present. It is enough to point out that at least there would be a *very serious question* to be answered *before* Mrs. Frick and Miss Frick could be made to pay a tax on the transfer of his estate by Mr. Frick. There would be *another* if the provisions for the liability of beneficiaries were held to be separable and it was proposed to make the estate pay a transfer tax for property that Mr. Frick did not transfer." (Italics ours.)

In the case at bar, the United States under the 1921 Revenue Act, exacted $9,146.76 from Mr. Brown's estate on account of $160,888.21 which his estate did not own, which his executors never had, and over the payment of which they had no control. It is certainly a "direct" tax, not apportioned, and hence void.

C.

The tax of $9,146.76 is not an "excise" tax within any definition ever suggested by this Court.

The right of Congress to levy an inheritance tax without apportionment has been upheld by this Court (*Knowlton* v. *Moore*, 178 U. S. 41). The refined theory upon which this decision was rested can be properly appreciated and considered only by an understanding of the judicial history of the times immediately preceding the decision of the case.

In *Scholey* v. *Rew*, 23 Wall. 331 (1874), this Court held that a tax in respect of any disposition of real estate by will, deed or laws of descent, to become effective upon death, was a tax on the right to become the successor of real estate on the death of the person whose interest was acquired and that therefore such tax was an excise tax on the devolution of the title, and was not a direct tax.

Some twenty years later this Court, in *Pollock* v. *Farmers Loan & Trust Company*, 157 U. S. 429 (1894), apparently rejected the reasoning by which this Court in *Scholey* v. *Rew* had reached its decision and it was thereafter considered that the latter case had been overruled.

This was the condition of the law when *Knowlton* v. *Moore* (178 U. S. 41) came up for decision, and this Court held that the 1898 Inheritance Tax Law imposed a tax not on the net estate, but on the legacy or distributive shares of personal property only and that the tax was not a direct tax, but was an excise tax in the nature of a death duty. In the course of its opinion the Court, by Mr. Justice White, later Chief Justice, laid down the following propositions:

I. That under the practice of many nations some form of death duty was a well known method of taxation, whether

called probate or stamp duty, legacy or estate tax, etc., that in all countries such taxes (p. 56)

> "rest in their essence upon the principle that death is the generating source from which the particular taxing power takes its being, and that it is the *power to transmit*, or the transmission from the dead to the living, on which such taxes are more immediately rested" (Italics ours);

and that under the broad power "to lay and collect taxes, duties, imposts and excises," Congress could levy the tax commonly called an inheritance tax (pp. 47-61).

II. That, generally speaking, such death duties have in all countries been considered as different from taxes levied on real or personal property by reason of the ownership or possession thereof; and that, historically, Congress had, in the legislation of 1797, 1862-1866, and 1894, treated death duties as indirect taxes.

III. That *Scholey* v. *Rew* was not overruled by the *Pollock* case, and hence an inheritance tax, by virtue of that decision, must be deemed an excise tax and not a direct tax.

The basis of the Government's contention that the tax in the instant case is valid is the theory that it is an excise tax, and great reliance is placed by the Government upon *Knowlton* v. *Moore*. We submit that an examination of the Court's opinion in *Knowlton* v. *Moore* will demonstrate that the tax complained of here can in no way be considered an excise tax. The Court in the *Knowlton* case stated, at page 57:

> "Confusion of thought may arise unless it be always remembered that, fundamentally considered, it is *the power to transmit or the transmission or receipt of property by death* which is the subject levied upon by all death duties" (Italics ours).

And again, at page 59:

> "The thing forming the universal subject of taxation upon which inheritance and legacy taxes rest is the

transmission or receipt, and not the right existing to regulate". (Italics ours.)

And again, at page 47:

"Taxes of this general character are universally deemed to relate, not to property *eo nomine*, but to its passage *by will or by descent* in cases of intestacy, as distinguished from taxes imposed on property, real or personal, as such, because of its ownership and possession. In other words, the public contribution which death duties exact is predicated on the *passing of property as the result of death*, as distinct from a tax on property disassociated from its transmission or receipt by will, or as the result of intestacy." (Italics ours.)

And again, at page 56:

"Although different modes of assessing such duties prevail, and although they have different accidental names, such as probate duties, stamp duties, taxes on the transaction, or the act of passing of an estate or a succession, legacy taxes, estate taxes or privilege taxes, nevertheless tax laws of this nature in all countries rest in their essence upon the principle that death is the generating source from which the particular taxing power takes its being and that it is the *power to transmit*, or the *transmission from the dead to the living*, on which such taxes are more immediately rested." (Italics ours.)

In *Hertz* v. *Woodman*, 218 U. S. 205, 219, the subject of the tax was thus stated:

"Now, *what is* the property, right or thing which is made subject to the tax? This has been most conclusively answered by *Knowlton* v. *Moore*, 178 U. S. 41, 56, where the section in question is construed as laying a tax upon the *transmission*, or *the right to succeed to a legacy*, or *distributive share or gift in contemplation of death*, passing after the act. • • •

To repeat then: The subject of the tax or duty exacted by § 29 is the *right of succession which passes by death* to a vested beneficial right of possession or enjoyment to a *legacy* or *distributive share*." (Italics ours.)

In *New York Trust Co.* v. *Eisner*, 256 U. S. 345, 349, the 1916 Act taxing net assets of the estate was sustained as an excise tax, the Court saying, with respect to the attempted distinction between a tax on the privilege of bequeathing and privilege of receiving:

> "But that matter also is disposed of by *Knowlton* v. *Moore*, not by an attempt to make some scientific distinction, which would be at least difficult, but on an interpretation of language by its traditional use—*on the practical and historical ground that this kind of tax always has been regarded as the antithesis of a direct tax*; 'has ever been treated as a duty or excise, because of the particular occasion which gives rise to its levy.' 178 U. S. 81 83. Upon this point a page of history is worth a volume of logic." (Italics ours.)

In *Y. M. C. A.* v. *Davis*, 264 U. S. 47, 50, it was said of the 1918 Act there involved:

> "What was being imposed here was an excise upon the transfer of an estate *upon death of the owner*. It was not a tax upon succession and receipt of benefits under the law or the will. It was death duties as distinguished from a legacy or succession tax. What this law taxes is not the interest to which the legatees and devisees succeeded on death, but the *interest which ceased by reason of the death*. *Knowlton* v. *Moore*, 178 U. S. 41, 48, 49." (Italics ours.)

In *Edwards* v. *Slocum*, 264 U. S. 61, 62, it is said of the same Act:

> "But this is not a tax upon a residue. It is a tax upon a transfer *of his net estate by a decedent*, a distinction marked by the words that we have quoted from the statute, and previously commented upon at length in *Knowlton* v. *Moore*, 178 U. S. 41, 49, 77. It comes into existence before and is independent of the receipt of the property by the legatee. It taxes, as Hanson, Death Duties, puts it in a passage cited in 178 U. S. 49, 'not the interest to which some person succeeds on a death, but *the interest which ceased by reason of the death*.' It

levies a sum equal to a certain percentage of the value of the net estate, and provides the criteria by which the net estate shall be ascertained." (Italics ours.)

The numerous decisions of this Court in Federal Inheritance Tax cases establish the following propositions:

1. That the Federal inheritance tax—whether a legacy tax as in the 1898 Act or a net estate tax as in the 1921 Act—was held to be an excise solely because it was imposed upon the interest of the decedent which ceased by reason of death and thereupon passed to a beneficiary—from the dead to the living.

2. The property with respect to which the tax is imposed, must be property of the decedent, who directed its disposition after his own death either (1) by intestacy, will, or deed to take effect at death or (2) by conferring a power of appointment on another to dispose of it at such other's death.

3. The sole basis of sustaining such taxes as "excises" is that there is no inherent right in a decedent to direct the disposition of his property after his death; and that as the state alone authorizes or protects such disposition, it can attach to such privilege any conditions it chooses and that the Federal tax is simply imposed on the exercise of the privilege.

Taking these propositions in their order it is clear beyond any possibility of doubt that the tax complained of in this case does not come within the definition of an "excise" tax:

1. Mr. Brown had no interest which could or did cease at his death and no interest passed from him to any beneficiary upon his death since their interest in the policies had vested in them some years previous to Mr. Brown's death.

2. Mr. Brown neither owned the policies nor did he exercise by will or deed to take effect at death, any rights of ownership over these policies; he neither disposed of them

nor authorized another to dispose of them; there was no cessation of his interest upon his death and no transfer of such interest to another since the property rights in the policies were already in the beneficiaries prior to his death.

3. The falling in of these insurance policies upon Mr. Brown's death was not in any sense the exercise of a privilege granted by the state. A contract to pay money was merely performed. This was no tax on a privilege, it was a tax on the inherent and essential element of ownership, i. e., the right to take possession of one's own property and as such was a tax on property. In every inheritance tax case that has ever been decided by this Court, whether involving a State or Federal statute, the tax has been with respect to an estate that passed from the dead to the living, i. e., an estate that actually belonged to A and passed from him to a beneficiary either (1) at A's death by intestacy, will or trust deed to take effect upon his own death, or (2) at the death of B pursuant to some power of appointment conferred by A on B to take effect at B's death and exercised by B, which exercise by B this Court held was the cause of the transfer of the estate from the dead to the living.

An entirely different situation is presented in this case. The tax here contested is not imposed in respect of any estate of Mr. Brown passing on his death, either by will, deed, power of appointment or the intestate laws of the State or with respect of any legal privilege of taking his estate. The subject of the tax (the policies) did not pass from Mr. Brown at his death. The rights of the beneficiaries vested prior to Mr. Brown's death and his death merely fixed the time for the performance of the contract. A 6% tax on these policies can by no stretch of the imagination be termed an excise tax. It is a direct tax on property which has none of the elements of an inheritance tax, a death duty, a succession tax or any other kind of "excise" tax.

Question I certified should, therefore, we submit, be answered in the affirmative.

SECOND POINT: QUESTION II.

The tax of $9,146.76 imposed upon life insurance owned by surviving beneficiaries is so unreasonably determined that it is void, even though considered as an excise tax: Question II should, therefore, be answered in the affirmative.

The tax contested here lacks equality, universality and uniformity. In order fully to appreciate the nature and incidence of the tax we invite the Court's attention to the following elements:

1. The Statute arbitrarily makes something a part of Mr. Brown's estate which is not part of it;

(a) The property rights of the beneficiaries in the policies vested when the policies were taken out and the proceeds under the policies belonged absolutely to the beneficiaries.

(b) Mr. Brown during his lifetime could not gain possession of the proceeds of these policies, nor could he by his will exercise rights of ownership over these proceeds.

(c) The Plaintiff Executors of Mr. Brown's estate had no right or power over the proceeds.

2. The tax is assessed in this instance on Mr. Brown's estate.

3. The Statute attempts to give the Executors a cause of action against the beneficiaries to recover the amount of tax paid.

(a) The cause of action is inadequate since the Executors under the Statute cannot recover from the beneficiaries the full amount of the tax paid by reason of these proceeds.

(b) A mere cause of action to recover a part of the tax paid is not the equivalent of immunity from taxation.

This Court has repeatedly held that the constitutional limitations on the power of taxation must be strictly complied with and that the power to tax cannot be made the means of imposing upon one man the burden which should be borne by another.

In *Loan Association* v. *Topeka*, 87 U. S. 655, the Court condemned a state tax for private purposes, and Mr. Justice Miller writing for the Court, at pages 663-664, said:

> "There are limitations on such power which grow out of the essential nature of all free governments. • • • No court, for instance, would hesitate to declare void a statute • • • which should enact that the homestead now owned by A should no longer be his, but should henceforth be the property of B.
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> Of all the powers conferred upon government that of taxation is most liable to abuse.
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> • • • • • •
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> To lay with one hand the power of the government on the property of the citizen, and with the other to bestow it upon favored individuals to aid private enterprises and build up private fortunes, is none the less a robbery because it is done under the forms of law and is called taxation. This is not legislation. It is a decree under legislative forms."

Mr. Justice Hunt writing for the Court in *United States* v. *Baltimore & Ohio R. R. Co.*, 84 U. S. 322, said, at page 326:

> "It is not taxation that government should take from one the profits and gains of another. That is taxation which compels one to pay for the support of the Government from his own gains and of his own property."

In *Hartman* v. *Greenhow*, 102 U. S. 672, the State of Virginia endeavored to collect a tax on its own bonds out of interest payable on detached coupons. This Court unequivo-

cally condemned this form of legislative irresponsibility and said, in the opinion of Mr. Justice Field, at page 684:

> "* * * surely it is not necessary to argue that an act which requires the holder of one contract to pay the taxes levied upon another contract held by a stranger cannot be sustained. Such an act is not a legitimate exercise of taxing power; it undertakes to impose upon one the burden which should fall, if at all, upon another."

Does not the tax complained of here possess the very elements which have been so frequently and so forcefully criticized and condemned by this Court?

The property upon which the tax is based is not part of Mr. Brown's estate. It is not and has never been in the hands of the Executors. Neither the estate nor the Executors have anything to do with it. They could not help the beneficiaries to get it. They could not prevent the beneficiaries from getting it. They are as negligible in the payments of amounts of life insurance as if Mr. Brown had left no estate at all and had neither an executor nor an administrator.

To compel the Executors to pay a tax on the proceeds of these policies is not taxation at all. It is confiscation. It is the taking of property for public use without compensation and without due process of law, and in its very essence, we submit, violates the Fifth Amendment of the Constitution.

The Government in its brief in the court below stated that if the measure of an excise tax bears a reasonable relation to the subject matter of the tax, the tax is valid, and in support of this statement the Government cited the following cases: *License Tax Cases*, 5 Wall. 462, 471; *United States* v. *Singer*, 15 Wall. 11, 121; *Knowlton* v. *Moore*, 178 U. S. 41, 57, 58; *Patton* v. *Brady*, 184 U. S. 608, 619, 620, 622; *McCray* v. *United States*, 195 U. S. 27, 59, 60, 63; *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 158; *Billings* v. *United States*, 232 U. S. 261, 281, 282; *Brushaber* v. *Union Pacific R. R. Co.*, 240 U. S. 1, 20, 24; *United States* v. *Doremus*, 249 U. S. 86, 93.

An examination of these cases discloses that neither the

License Tax Cases nor *Billings* v. *United States* are in point for the proposition stated.

In *United States* v. *Singer* the excise was measured by the capacity of the *taxpayer's* distilleries.

Knowlton v. *Moore* held a legacy tax imposed by the War Revenue Act of 1898 to be an excise tax and specifically rejected the theory that the tax should be measured by the size of the entire estate.

Patton v. *Brady* involved an excise tax on tobacco purchased, held or intended for sale, and the tax was measured on the basis of the amount of tobacco in the *taxpayer's* possession or under his ownership.

McCray v. *United States* concerned an excise tax on the manufacture or sale of oleomargarine and the tax was measured by the amount and character of the oleomargarine manufactured or sold by the *taxpayer*.

In *Flint* v. *Stone Tracy Co.* the excise tax under the Corporation Tax Law of 1909 upon nontaxable property was measured by income to the corporation and not by income from a stranger's property or from property owned in the past.

Brushaber v. *Union Pacific Railroad Co.* involved the provisions of the Tariff Act of October 3, 1913, and the Court held that the tax on the franchise privilege was properly measured by income earned by the corporation in the preceding year.

United States v. *Doremus* concerned a tax on the manufacture or sale of opium, drugs, etc. under the Narcotic Drug Act of December 17, 1914. The tax was measured by the amount of opium, drugs, etc. manufactured or sold by the *taxpayer*.

In none of the foregoing cases relied upon by the Government was a tax levied or attempted to be levied on property of A measured by the property of B.

The Government further stated in its brief in the court below that "an excise tax may be measured by property or

transactions which would in themselves not be taxable". In support of this proposition the following cases were cited: *Greiner* v. *Lewellyn*, 258 U. S. 384; *Maxwell* v. *Bugbee*, 250 U. S. 525; *Flint* v. *Stone Tracy Co.*, 220 U. S. 107; *Orr* v. *Gilman*, 183 U. S. 278; *Plummer* v. *Coler*, 178 U. S. 115; *United States* v. *Perkins*, 163 U. S. 625.

On the authority of these cases the Government contended that no constitutional limitation was violated by that portion of the Revenue Act of 1921 which required that there should be included in the gross estate of the decedent for Federal Estate Tax purposes proceeds of insurance policies in excess of $40,000 on the decedent's life and payable to beneficiaries other than the estate. We respectfully submit that the cases cited by the Government are not in point and are no authority for the conclusion which the Government attempted to draw.

For example, in *Greiner* v. *Lewellyn*, 258 U. S. 384, the Court held that in imposing a tax on the transfer of an estate by death Congress has power to require that state and municipal bonds forming part of the estate shall be included in determining the net value of the estate by which the tax is measured. The municipal bonds in that case were in fact *owned by the decedent at the time of his death*.

In *Maxwell* v. *Bugbee*, 250 U. S. 525, the Court held that the State of New Jersey could impose a tax on the succession of the personal representative in New Jersey to a nonresident's local property and could measure that tax by property outside of the state and beyond its taxing jurisdiction. The property outside of New Jersey which was considered in determining the rate of tax in that case was property of the decedent at the time of his death and not property which had theretofore been conveyed away by him.

In *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, it was held that a Federal excise tax on corporations for the privilege of doing business in a corporate capacity was valid, although the tax was measured by the income of the corporation from

sources which included interest on Government securities and other properties, the income of which could not be taxed. The income from such nontaxable property by which the excise tax in that case was measured was income to the corporation and *not income from a stranger's property*.

In *Orr* v. *Gilman*, 183 U. S. 278, this Court sustained the New York Court of Appeals in holding that the exercise of a power of appointment as a matter of law was an act essential to the passing of title and that a privilege exercised by the decedent at his death by will might properly be measured by the value of the property passing, even if such property consisted of securities exempt by statute from tax.

In the case of *Plummer* v. *Coler*, 178 U. S. 115, wherein the State of New York imposed a tax on a legacy which consisted of nontaxable Government bonds, the Court held that the tax, being an excise tax on the exercise of a right or privilege, the State could lawfully measure or fix the amount of the tax by referring to the value of the property passing, and that the tax was not invalidated because the property which passed was in whole or in part tax exempt Government bonds.

In *United States* v. *Perkins*, 163 U. S. 625, the Court held that although the property of the United States cannot be taxed by a state, nevertheless an inheritance tax imposed by the State of New York on a bequest by will to the United States could properly be levied upon such gift.

There are doubtless numerous other decisions of this Court and other Courts sustaining excise taxes which are measured by the value or extent of tax-exempt property or property which would not of itself be taxable. It will be observed from an examination of these cases that the property which is there used as a measure of the tax is property belonging to the taxpayer against whom the tax is assessed.

We do not contend that Congress is without power to prescribe that an excise tax may be measured by including in the measure of the tax, property which would otherwise not be taxable. Such a proposition has frequently been stated by this Court. But there is no suggestion in any language ever

used by this Court that Congress has power to impose a tax on A measured by property which does not belong to A and over which A has no control, but which belongs exclusively to B.

If Mr. Brown's estate had consisted entirely of Government tax-exempt securities we concede that the measure of the Federal Estate Tax on Mr. Brown's estate would include the value on the date of his death of all such tax-exempt securities.

To say that the measure of an excise tax may include non-taxable property is one thing; but to say that the measure of a tax on a privilege exercised by A may include property which A did not own, which never could be part of his estate but which was owned exclusively by B is quite a different thing. The latter proposition would appear to be self-evident.

As the Court said in *Wardell* v. *Blum*, 276 Fed. 226, at page 227, holding that in an estate of a resident of California only one-half of the community property is subject to Federal Inheritance Tax under the Revenue Act of 1916:

> "All inheritance taxes are imposed on the transfer of the net estate of the 'deceased'; from which the conclusion is inevitable that the property upon which such a tax is imposed must, in truth, be the property of the deceased."

That Congress cannot constitutionally measure a tax on A by property which A does not own but which belongs exclusively to B was declared and emphasized in the recent case of *Free* v. *Bowers*, 12 Fed. 2nd, 625, decided in the Circuit Court of Appeals for the Second Circuit in June, 1928. In that case by the will of one Alice J. Nash, probated in 1904, a trust was created for the benefit of her husband, William A. Nash, for life, with remainder in trust for life as to one part thereof for a son; upon the son's death that part vested in his children or more remote descendants. The remaining part of the trust was similarly limited to and in a daughter and her

children or more remote descendants. In 1910 the life tenant, William A. Nash, who was also one of the trustees, conveyed to the trustees securities then valued at $200,000 to be held subject to the terms of the trust as defined in the will of Mrs. Nash. No power of revocation was reserved by Mr. Nash as to the securities placed in the trust. These securities were treated by the trustees as part of the trust and by 1922 they had increased in value to upwards of $500,000. Mr. Nash died in 1922 and the Commissioner of Internal Revenue included in his gross estate for purposes of levying an estate tax under the Revenue Act of 1921, the 1922 value of the securities. The Executors paid the tax under protest and sued to recover it back. The District Court found for the defendant, but on appeal the Circuit Court reversed the judgment and held that the Revenue Act of 1921 if construed to include in the gross estate of Mr. Nash the securities which he had delivered to the trustees in 1910, was unconstitutional. In the course of the opinion, Hough, *C. J.*, says at page 12:

> "Thus we must first decide whether within the meaning of the Statute Mr. Nash at the moment of his death had any *interest* within the meaning of the Act. We incline to hold that the applicable words should be treated technically and that therefore there was no *interest* left from or arising out of the gift computed in 1910 • • •
>
> But if the technical construction is wrong, then we must face the question whether it is within the power of Congress to do what has been done; *i. e.*, use the property of A as a measure for the tax to be laid upon B. Thus stated it would seem impossible to support the tax • • •
>
> If that description be accepted, while there is no classification of taxpayers, the tax itself is 'arbitrary and capricious'. *Barclay v. Edwards*, 267 U. S. 442, 450; 45 S. Ct. 135, 348 (69 L. Ed. 703). Further a tax on a transfer by A but measured by anything other than the estate of A may be a duty or excise in form, but it is a palpable effort to tax something other than the transfer. • • •
>
> If it be said that Congress might have taxed the 1910 transfer, and therefore can tax it even in 1922, the

answer is that nothing of the kind has been attempted. There is no tax now laid on the transfer of 1910, nor the property transferred. Could Congress in 1922 have laid a tax on Mr. Nash because he gave away $200,000 in 1910? If that be assumed as possible, it is not possible that the tax so laid, and computed on the gift, its credits and gains, could ever be an excise on the transfer.

But if the tax be laid as it actually has been, and called an excise on the transfer of something else, the name is merely false, there is no excise, and the exaction falls into the category of unapportioned direct taxes. We think this an effort to use a constitutional power as a hook on which to hang a cloak that conceals unconstitutional action. There is no real difference between disguising this direct tax under the name of a duty, and laying a tax in order generally to regulate some subject taxable, but not otherwise subject to national regulation. The real purpose is dealt with, notwithstanding the cloak. *The Child Labor Cases*, 259 U. S. 20, 42 S. Ct. 449, 66 L. Ed. 817, is the leading example.

It follows that we think there was no 'interest' shown in Mr. Nash, justifying the tax laid; but, if the statute required the tax as laid, then the exaction was arbitrary and unconstitutional."

Of course, the Revenue Act of 1921 attempts to give the executors a right to recover from the beneficiaries of the insurance a *portion* of the tax paid. Obviously if the executors had no recourse against the beneficiaries of the policies for the tax paid on the amount of their proceeds the tax would plainly be invalid. There must be some basis for taxation. Normally it is found in the protection accorded by the taxing power to the subject of the tax. The subject can be taxed differently from others only when he belongs to a class which may be differentiated from those others, or owns something which those others do not own, or does something which those others do not do, or benefits by something by which those others do not benefit. The Executors of the estate of Mr. Brown cannot be distinguished from other executors and estates by reason of the policies of insurance not payable to them which are here involved, which they do not

own, with reference to which they did nothing and could do nothing and by which they did not in any way benefit.

The most that can be said in favor of the tax here in question is that it is a tax on the amount received by Mrs. Brown and her two children and that the Executors are made the collectors of the tax for the United States. We invite the attention of the Court, however, to the fact that the Act attempts to give the Executors the right to recover *only* a *part* of the amount which the estate has to pay. For example in this estate the tax which the United States has levied by reason of the inclusion in the gross estate of proceeds of insurance policies taken out by Mr. Brown on his own life and payable to beneficiaries other than the estate is $9,146.76. It is to be noted that the Plaintiff Executors have the right to recover such portion of the total tax paid as the proceeds in excess of $40,000 of such policies bear to the net estate. As pointed out on page 5 of this brief, the Executors could recover from the beneficiaries $5,927.16 instead of the actual amount of the tax paid by reason of these insurance policies or $9,146.76. This leaves $3,219.13 to be borne by the Executors, or 35.17 per cent of the tax on the insurance.

A few simple illustrations will suffice to demonstrate the inequality and lack of uniformity of the tax contested.

1. Suppose a decedent leaves a net estate of $50,000 and insurance policies payable to beneficiaries other than his estate amounting to $140,000. Under the Revenue Act of 1921, as construed by the Government, the tax would be calculated as follows:

1% of $50,000	$500
2% of 100,000 (the proceeds of the insurance over $40,000)	2,000
Total tax	$2,500

The executors are required to pay the entire tax. They are given the right to recover from the beneficiaries of the insur-

ance policies $1,666.66, leaving $333.34 to be borne by the recipient of the decedent's net estate.

In other words, if A dies leaving a net estate of $50,000 and no insurance, the recipient of that net estate pays a tax (through the executors) of $500.

But if B dies leaving a net estate of $50,000 and insurance policies payable to beneficiaries other than the estate of $140,000, the recipient of B's net estate pays a tax (through the executors) of $833.34. This increased tax arises by reason of the fact that Congress has prescribed in the Revenue Act of 1921 that the tax on B's estate shall be computed by including in B's estate something that never was a part of it.

2. Suppose a decedent dies leaving a net estate of $1,000,000 and insurance policies payable to beneficiaries other than the estate of $140,000. The tax would then be computed as follows:

1% of $50,000	$500
2% of 100,000	2,000
3% of 100,000	3,000
4% of 200,000	8,000
6% of 300,000	18,000
8% of 250,000	20,000
Total	$51,500

to which must be added the proceeds of the insurance policies in excess of $40,000 at the rate of 10%, or

10% of $100,000	10,000
	$61,500

In this illustration the executor has the right under the 1921 Act to recover from the beneficiaries of the insurance policies $5,590.90 of the tax arising by reason of such proceeds, leaving $4,409.10 of such tax to be borne by the recipients of the decedent's net estate.

It is to be noted that in the first example the beneficiary of insurance policies aggregating $100,000 pays a tax of $1,666.66. In the second illustration the beneficiary of insurance policies of exactly the same amount pays a tax over three times as large, or $5,590.90 and all by reason of the fact that in the second example the decedent happened to be a wealthy man.

Where is the equality in taxation of this kind, if it can be dignified by the term "taxation" at all? The proportion of the insurance tax recoverable by the executors under given conditions is governed not by any consistent rule of policy, logic or convenience, but by the sheerest caprice.

3. But consider the result if a decedent dies leaving no net estate of his own property, but insurance policies payable to beneficiaries other than his estate aggregating $1,040,000. The tax on the "estate" would be $51,500. Under the Act of 1921 the executors, having no assets whatever, would be legally obligated to pay into the treasury of the United States the sum of $51,500. Just how such a transaction would be financed is difficult to understand.

4. Or suppose in the last illustration, that the decedent died leaving no estate of his own and in debt $250,000. The tax on the "net estate" would then be $31,500 which the executors in the first instance would have to pay. Under these circumstances consider what happens under the method prescribed by the Statute for the recovery by the executors of the tax so paid. Mathematically expressed it would be as follows:

$$X = \$31,500 \times \$1,000,000 - \$750,000$$

In other words under the terms of the Statute the executors would be entitled to recover from the beneficiaries of the insurance policies a sum which would be in excess of the tax paid, the recovery by the executors in this instance would be $42,000.

Further illustration would seem to be superfluous. The portion of the 1921 Revenue Act in question here is an extraordinary example of legislative recklessness and we submit deserves the condemnation of this Court, which has in the past declared void and unconstitutional taxing statutes which had the effect of making one man pay another man's tax. Upon analysis it seems conclusive that the tax imposed bears a highly unreasonable relation to the subject matter of the tax. It is not uniform, it is not universal, it is not equal. It is the deprivation of property without due process of law and without compensation and amounts in our submission to confiscation of property.

A somewhat similar, but less obvious, situation was presented in *Knowlton v. Moore*, wherein the Government contended that the brackets of the progressive inheritance tax rates were to be determined not by the amount of each legacy, but by the total estate of the decedent. In rejecting that construction, the Court said at page 76:

> "The principle on which such construction rests was thus defended in argument. The tax is on each separate legacy or distributive share, but the rate is measured by the whole estate. In other words, the construction proceeds upon the assumption that Congress intended to tax the separate legacies, *not by their own value, but by that of a wholly distinct and separate thing.* But this is equivalent to saying that the principle underlying the asserted interpretation is that the house of A, which is only worth one thousand dollars, may be taxed, but that the rate of the tax is to be determined by attributing to A's house the value of B's house, which may be worth a hundredfold the amount. The gross inequalities which must inevitably result from the admission of this theory are readily illustrated. Thus, a person dying, and leaving an estate of $10,500, bequeaths to a hospital $10,000. The rate of tax would be 5%, and the amount of tax $500. Another person dies at the same time, leaves an estate of $1,000,000, and bequeaths $10,000 to the same institution. The rate of tax would be 12½ per cent., and the amount of the tax $1,250. It would thus come

to pass that the same person, occupying the same relation, and taking in the same character, two equal sums from two different persons, would pay in the one case more than twice the tax that he would in the other. In the arguments of counsel tables are found which show how inevitable and profound are the inequalities which the construction must produce. Clear as is the demonstration which they make, they only serve to multiply instances afforded by the one example which we have just given. • • •

It may be doubted by some, aside from express constitutional restrictions, whether the taxation by Congress of the *property of one person*, accompanied with an arbitrary provision that the rate of tax shall be fixed *with reference to the sum of the property of another*, thus bringing about the profound inequality which we have noticed, would not transcend the limitations arising from those fundamental conceptions of free government which underlie all constitutional systems. On this question, however, in any of its aspects, we do not even intimate an opinion, as no occasion for doing so exists, since, as we understand the law, we are clearly of opinion that it does not sustain the construction which was placed on it by the court below."

A colorable excuse might be found for taxing the legacies given by a decedent, at rates proportioned upon the size of his estate; but how can *any* excuse be found for taxing A on *his own* property at a rate determined by B's estate?

In *Frick* v. *Lewellyn*, 298 Fed. 803, the District Court said on this subject at page 811:

> "• • • Gross inequities and unjust discriminations would inevitably result from such a method of imposing taxes. Should the tax exceed the value of the property, the possessor would be given no right to surrender it to the taxing power in lieu of payment. The estate would not be protected by the provision for recoupment; such right of action could never be the equivalent of immunity from taxes, even if an action would lie, by the executors, for the full amount paid, because of the uncertainties of

enforcing judgment. Conspicuously is this true in the Act under consideration, because it imposes a liability on the executors for the full amount of the taxes, and at the same time only enables them by action to recover a part. Not only so, but the amount of the tax depends, not upon the value of the policies, or the total amount of all the policies, but upon the amount of the dead man's estate, plus the value of the policies.

In *Knowlton* v. *Moore*, *supra*, which involved the interpretation of the War Revenue Act of 1898 (30 Stat. 448), where taxes has been collected on certain legacies and distributive shares, the rate being fixed, not on the amount coming to each individual, but on the whole personal estate. Chief Justice White condemned such method in these words:

> 'But this is equivalent to saying that the principle underlying the asserted interpretation is that the house of A, which is only worth one thousand dollars, may be taxed, but that the rate of the tax is to be determined by attributing to A's house the value of B's house, which may be worth a hundredfold the amount. The gross inequalities which must inevitably result from the admission of this theory are readily illustrated.'

In the same spirit and with the same thought in mind, in *Hartman* v. *Greenhow*, in 102 U. S. 672, 26 L. Ed. 271, which involved the validity of a statute requiring a tax on bonds to be deducted from coupons, which were detached and held by different owners, Mr. Justice Field said:

> 'Surely it is not necessary to argue that an act which requires the holder of one contract to pay the taxes levied upon another contract held by a stranger cannot be sustained. Such an act is not a legitimate exercise of the taxing power; it undertakes to impose upon one the burden which should fall, if at all, upon another.'

In obedience to the authorities and the principles of law as I understand them, I am constrained to hold that the imposition and collection from the plaintiffs of $108,657.38, the amount of the tax in question, was without

authority of law and in violation of the plaintiffs' constitutional rights, and that judgment for that amount should be entered for the plaintiffs, with interest and costs, and it is accordingly so ordered."

No argument can escape the bare fact that the tax on the surviving beneficiary of the policy is determined by the wealth of the insured decedent. If Mrs. Brown and the Brown children were taxed at the "estate tax" progressive rates, on the insurance received, they would pay about $1500 and $750 each respectively, or $3,000 in all. But merely because they held insurance on a well to do man's life the tax is $9,146.76.

Conclusion.

Congress undoubtedly has the constitutional power, as Section 401 of the Revenue Act of 1921 enacts, to impose a tax "upon the transfer of the net estate" of the Plaintiffs' decedent, but the Plaintiffs submit that the proceeds of the insurance policies which the Commissioner of Internal Revenue added to Mr. Brown's net estate under § 402(f) of the Act were never a part of his estate, and that the imposition of an "estate tax" on these proceeds or on the "net estate" including these proceeds is a violation of Article I and the Fifth Amendment of the Constitution of the United States.

We respectfully submit that Question I and Question II certified to this Court by the Court of Claims of the United States should both be answered in the affirmative.

Respectfully,

DALLAS S. TOWNSEND,
HENRY WALTON PROFFITT,
For the Plaintiffs.

[redacted]

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Supreme Court of the United States

OCTOBER TERM, 1928. No. 77.

THE CHASE NATIONAL BANK, ET AL.,
EXECUTORS, - - - - - - - - *Plaintiffs,*

vs.

THE UNITED STATES, - - - - - - *Defendant.*

On Certificate from the Court of Claims.

BRIEF IN SUPPORT OF THE PROPOSITION.

That the "Estate Tax" imposed by the Revenue Act of 1921 is void, because (1) it is a direct tax, and (2) it is arbitrary and capricious.

The two certified questions arise under §402(f) of the Federal Estate Tax provisions of the Revenue Act of 1921 (42 Stat. 227); and the Court of Claims asks whether a $9,146.76 tax, imposed thereunder in respect of $160,888.21 of life insurance payable directly to a widow and children as beneficiaries, (1) is a *direct* tax on property and void because not apportioned, or (2) bears such an unreasonable relation to the subject matter of the tax as to render it void (R. 7). These are the same questions that were presented, but not decided, in *Lewellyn* v. *Frick*, 268 U. S. 238, 251.

STATEMENT OF THE CASE.

1. *Brown's $200,000 insurance and death.* In September, 1922, Brown, aged 45, insured his life for $200,000 by three policies payable to his wife as beneficiary, reserving the right to change the beneficiary (R. 4). Two weeks later, acting under that reserved power, he changed a $100,000 policy from his wife to his two children as beneficiaries (R. 4). The policies also gave to Brown the right (without the necessity of his obtaining the beneficiaries' consent thereto), (1) after three full years' premiums were paid, to obtain certain loan or surrender values, and (2) to avail himself of certain other customary benefits varying slightly in the different policies (Policies at R. 14).

After paying $16,230 premiums for the first two years, he died in 1924; and the New York Life paid $200,888.21—one-half ($100,444.10) to the wife, and the other half ($100,444.11) to the children (R. 5).

2. *The Federal Estate Tax on the widow's and children's insurance.* Brown left a gross estate of

his own	$524,336.29
The Commissioner added thereto the insurance	$200,888.21
Total Gross Estate	$725,224.50
Lawful deductions for debts, etc. (including $40,000 statutory deduction of insurance)	$139,662.93
Net Estate	$585,561.57
The executors paid the full Federal Estate tax thereon (R. 6)	$21,691.66

The executors sued to recover $9,146.76, which is the amount of the tax paid with respect of the $160,881.21 life insurance included as part of Brown's net estate, *i. e.*, $200,888.21—$40,000 statutory exemption —$160,881.21 (R. 6).

Congress had, of course, the undoubted power to tax the $160,881.21; but the questions involved are *not* as to its *power to tax*, but whether it has *exercised* that power in accordance with the constitutional limitations of (1) apportionment and (2) due process.

3. *The relevant Federal estate tax statutes.* The Federal estate tax statute imposed a graduated percentage tax (§401)

> "*upon the transfer* of the net estate of every decedent."

The net estate was defined to be the gross estate *minus* certain deductions (§403). The gross estate was defined to include various properties, etc., and also (§402f)

> "to the extent of the excess over $40,000 of the amount *receivable by all other beneficiaries* as insurance under policies taken out by the decedent upon his own life."

In short, the net estate of a decedent was defined to include all the life insurance (above $40,000) which he took out on his life payable to his wife, children or other beneficiary; and the tax upon the supposed transfer thereof was fixed at the highest

bracket,—determined, not by the amount of insurance the beneficiaries received, but solely by the size of the decedent's total net estate, so that a small amount of life insurance (over $40,000) payable to a dependent mother, sister or child, might be taxed 25%, if the decedent happened to be a very wealthy man.

The statute required the Executor to pay the tax and made both him and the beneficiaries personally liable therefor (§406-409).

If the Executor pays the tax, he can recover from the beneficiaries "such portion of the total tax paid as the proceeds, in excess of $40,000, of such policies bear to the net estate" (§408); or expressed arithmetically:

Executor's Recovery	Total Tax	Proceeds over $40,000	Net Estate
X	$21,633.69	$160,888.21	$585,561.57

The tax is to be borne as follows:

Widow and children	64.83%	$5927.63
Executors	35.17%	3219.13
Tax in dispute	100.00%	$9146.76

The effect of the statute is this:

Mr. Brown's widow and children must bear $5927.63 tax, solely because they are beneficiaries of $200,000 life insurance.

The Executors must bear $3219.13 tax, solely because Mr. Brown insured his life for his wife's and children's benefit.

It was exactly that situation which Justice HOLMES had in mind when he said in *Lewellyn* v. *Frick*, 268 U. S. 238, 251:

> "It is enough to point out that at least there would be a very serious question to be answered before Mrs. Frick and Miss Frick could be made to pay a tax on the transfer of his estate by Mr. Frick. There would be another if the provisions for the liability of beneficiaries were held to be separable and it was proposed to make the estate pay a transfer tax for property that Mr. Frick did not transfer. Acts of Congress are to be construed if possible in such a way as to avoid grave doubts of this kind."

He meant to call attention to the fact (1) that if the Frick Executors tried to collect 88.56% of the $108,657.38 tax from Mrs. Frick and Miss Frick, it might be void; and (2) that even if such possibly void provision could be held separable (without automatically destroying the *whole section* as to insurance), it might still be unlawful to make the Frick estate bear the tax on property (insurance) that Mr. Frick did not transfer by his death.

Baldly stated, the Revenue Act of 1921 imposed a graduated Federal Estate tax "upon the *transfer* of the *net estate* of every decedent," and then assumes to include in such net estate, not only the decedent's own property but also life insurance which the decedent took out on his life, payable, *not* to his estate, but to other beneficiaries, *i. e.*, in this case, to his widow and children.

Fully conceding the power of Congress to tax the proceeds of life insurance policies, the questions presented as certified are:

1. Is the tax a direct tax?
2. Is it a violation of "due process" (*a*) to tax Mr. Brown's estate on account of money which his widow and children receive from an insurance company as indemnity for their loss in his death, and (*b*) to tax the widow's and children's insurance money on a sliding scale based on the size of Mr. Brown's estate?

SUMMARY OF POINTS DISCUSSED.

1. **The 1921 Federal Estate Tax is solely an excise tax upon the transfer of an estate from the dead owner to the living recipients.**
2. **Upon Brown's death, there was no transfer of $200,000 from him, as a dead owner, to a living recipient.**

   The $200,000 insurance was no part of Brown's estate; but, by the very nature of life insurance, it was the performance by the New York Life of its personal contract of indemnity to pay $200,000 to a widow and children as a substitute for the permanent loss they suffered in the death of their supporter and protector.
3. **The Federal Estate Tax as applied to the $160,888.21 life insurance paid by the New York Life to the widow and children is void because it is a "direct" tax and not apportioned.**
4. **The $9,146.76 tax on the life insurance owned by Mrs. Brown and her children is void because it was determined in so arbitrary and capricious a manner as to violate the due process clause of the Fifth Amendment.**

FIRST POINT.

The 1921 Federal Estate Tax is solely an excise tax upon the transfer of an estate from the dead owner to the living recipients.

The Federal Estate Tax laws of 1916, 1918, 1921, 1924, and 1926, use identic language in declaring that a percentage tax

> "is hereby imposed *upon the transfer of the net estate of every decedent,*" etc.

It must be noted that Congress has not attempted to impose a tax upon the transfer of property from A to B on X's death; but limits the tax to the transfer of X's property at X's death.

In response to various constitutional objections to such taxes, this Court has taken great pains to point out that the tax is not imposed on the property itself, nor on the residue of an estate, but that it is

> "an excise upon the transfer of an estate *upon the death of the owner.* * * * What this law taxes is * * * *the interest which ceased* by reason of the death" (*Y. M. C. A.* v. *Davis*, 264 U. S. 47, 50).
>
> "It is a tax upon a transfer of *his net estate by a decedent.* * * * It taxes * * * the interest which ceased by reason of the death" (*Edwards* v. *Slocum*, 264 U. S. 61, 62).
>
> "While the federal tax is called an estate tax, and the state tax is called a transfer tax, both are imposed as excises *on the transfer of property*

from a decedent * * *" (*Frick* v. *Pennsylvania*, 268 U. S. 498).

Similarly, the 1898 tax considered in *Knowlton* v. *Moore*, 178 U. S. 41, and *Hertz* v. *Woodman*, 218 U. S. 205, was a tax, not on the legacy at all, but upon the

"right to *succeed* to a legacy" (218 U. S. 219).

The two kinds of excise taxes, *i. e.*, (1) estate tax and (2) legacy tax, are thus aptly summarized in *Stebbins* v. *Riley*, 268 U. S. 137, 141, 144:

> "The subject matter of an inheritance taxing statute may be either *the transmission*, or the exercise of the legal power of transmission, of property *by will or descent* (*United States* v. *Perkins*, 163 U. S. 625, 629; *Plummer* v. *Coler*, 178 U. S. 115, 125; *New York Trust Co.* v. *Eisner*, 256 U. S. 345), or it may be the legal privilege of taking property by *devise or descent* (*Magoun* v. *Illinois Trust & Savings Bank*, 170 U. S. 283; *Knowlton* v. *Moore*, 178 U. S. 41; *Campbell* v. *California*, 200 U. S. 87). * * * There are two elements in every transfer of a *decedent's estate;* the one is the exercise of the legal power to transmit at death; the other is the privilege of succession. Each, as we have seen, is the subject of taxation."

The several expressions above were not loosely used, but were explanations deliberately and carefully framed in order to point out that the Federal Estate tax was in no sense a tax on the property it-

self, whether in the hands of the executor or of the legatee, nor was it a tax on the passage of title from A to B upon X's death, but it was either (1) a tax on the *transfer* of estate from the dead to the living [1921 Act], or (2) a tax on the privilege of receiving a legacy from a decedent [1898 Act.]

Nichols v. *Coolidge*, 274 U. S. 531, 537, 542, reiterates and emphasizes that the Federal estate tax is upon the transfer of property *from a decedent owner* to the recipients thereof.

These cases are clear and unmistakable declarations that what the 1921 Act actually did [irrespective of what Congress might do] was to tax *the transfer of the owner's (Brown's) estate*, which ceased at his death and passed to the beneficiaries. But, Brown had no interest in the $200,000. He had no interest therein which ceased at his death. There was no transfer of anything that he owned. The owners of the New York Life's promise to pay, to-wit: the wife and children, have not died. The only transfer that took place was that the New York Life transferred $200,000 from itself to the widow and children in settlement of its promise to pay the money when Brown died. The language of the 1921 Act does not reach such a transaction.

Bearing in mind, then, that the only thing on which the 1921 Federal estate tax constitutionally operates, as thus authoritatively determined by this Court, is the transfer of a *decedent's property by his death to the living recipient*, let us next inquire as to

the nature of the $200,000 insurance which the New York Life paid to the widow and children.

SECOND POINT.

Upon Brown's death, there was no transfer of $200,000 from him, as a dead owner, to a living recipient.

The $200,000 insurance was no part of Brown's estate; but, by the very nature of life insurance, it was the performance by the New York Life of its personal contract of indemnity to pay $200,000 to a widow and children as a substitute for the permanent loss they suffered in the death of their supporter and protector.

1. The $200,000 was paid by the New York Life out of its own corporate funds directly to the widow and children. It did not in anywise pass through or come out of Brown's estate. There was no transfer from Brown to the beneficiaries. No privilege of testamentary disposition or right to receive from a decedent's estate was involved.

2. The nature of life insurance is very simple and this Court has clearly defined it.

Life insurance is a method by which dependents are indemnified against the economic loss which results from the death of their supporter. Through a long series of years, Brown, and hundreds of thousands of other persons, of varying ages, severally made contracts with the New York Life, under which each person paid in annually a sum slightly in excess of his proportion of the risk of death, based upon his age and the character of the insurance desired.

Instead of each person paying each year a premium based on the mathematical probability of his death during that year, very low in the younger years, increasing slowly for many years, and then rising by leaps and bounds to prohibitive figures, so that in old age a member would pay almost the full face of the policy each year, it was long ago discovered that by a simple arithmetical calculation of interest, discount and the probability of dying, exactly the same result could be reached by the man paying the same sum each year, the over-payments in the earlier years being accumulated so as to provide a fund to take care of the greater cost in the later years.

This fund is called the Reserve. It is the mathematical sum necessary to be held to enable the company to pay its death losses as they occur. The moment it is impaired one dollar the company is insolvent. Its temparary accumulation is merely what the member pays for the advantage of not being compelled in old age suddenly to pay enormous sums each year for the current year's protection cost. In short, a member pays *in advance* for a part of the future protection, if he happens to live to old age. The New York Life received, invested and re-invested the money paid in, paid out taxes, expenses and the sums it promised to pay upon death, and after setting aside the legal Reserve (which, as above explained, is the amount required by law to be held for the future protection of policyholders and which is calculated by pure mathematics to the exact cent), what was left

over was returned at the end of each year to the policyholders in the shape of so-called "annual dividends," which were returned, as nearly as may be, in the proportions in which the policies contributed thereto. The policyholders got their insurance at cost, paying for it annually in advance; they paid a little more than they expected it would actually cost, in order to be sure that they paid in enough so that the common fund would not become insolvent, and they got back at the end of each year the amount so over-paid.

When a man takes out life insurance payable to his wife and children, it is not an accumulation of an estate, in which his interest ceases at his death, but such life insurance is a contract of indemnity, by which the company indemnifies the widow and children against the loss they suffer by the man's death. The man may or may not spend his income during life in providing for such indemnity. He may keep it up until his death, or he may drop it and let the indemnity lapse or cash in its "surrender value." When he dies, he possesses no interest which ceases and passes to the beneficiaries. There is no transfer of any estate from him to anyone else. There is nothing upon which the estate tax as an excise can operate. Such is the nature of life insurance.

This Court has held that such policies of life insurance are personal contracts, mere indemnity against loss, and are the substitution of money value

for the permanent loss suffered by the widow and children on the death of their natural supporter. (*N. Y. Life Ins. Co.* v. *Deer Lodge*, 231 U. S. 495, 508; *U. S.* v. *Supplee-Biddle Co.*, 265 U. S. 189, 195; *Central Bank of Washington* v. *Hume*, 128 U. S. 195, 205.)

Brown paid only $16,230 to the New York Life as premiums for the first and second years; and he then died before he even became entitled to borrow any money on the policies or to cash them in for their surrender value.

Although it had only received $16,230 from Brown, the New York Life performed its contract of indemnity; from its own corporate funds it paid out $200,000 to the widow and children. No part of the $200,000 was ever any part of Brown's estate. He never had any title to any part of it.

RESPONSE TO THE GOVERNMENT'S CONTENTIONS

The Government contends that because Brown paid the first two premiums out of his own funds, the $200,000 life insurance became a "savings investment," created and accumulated by him, and constituted a part of his estate, which was transferred at his death to the beneficiaries; and that, hence, it was properly subject to the Federal excise tax.

It is too obvious for argument that the $200,000 paid by the New York Life to the widow and children could not, in any aspect, be considered as a

"savings investment" created and accumulated in two years from $16,230!

To support its contention, the Government insists (1) that the policies belonged to Brown, who could at will assign them or change the beneficiary to his own estate; (2) that in bankruptcy their value would be an asset passing to the trustee; (3) that the State can subject policies, which are payable to a wife as beneficiary, to an insolvent husband's debts; (4) that in the popular mind a man's life insurance is considered a part of the estate which he "leaves" at the time of his death; and (5) that in England, since 1853, life insurance has been treated as subject to succession or death duties.

Let us consider those points in order.

(1) The policies were the New York Life's absolute promise to pay $200,000 to Mrs. Brown and her children, and their interest as beneficiaries was property of the most certain and valuable nature—a vested interest. They *owned* the New York Life's promise to pay. It was their property (*Washington Central Bank* v. *Hume*, 128 U. S. 195, 206).

But, the Government insists that a different rule obtains where, as here, the insured reserves the right to change the beneficiary, and that in such cases the beneficiary has no property right at all but only an expectancy (Brief, pp. 15, 16). The Government is simply wrong as to the law.

In each case, the beneficiary has a vested property ownership in the company's promise to pay; in the

one case, even the insured cannot disturb it, and while, in the other case, the beneficiary's rights are subject to be divested, if the insured exercises his right to change the beneficiary. But that reserved power *does not change the nature* of the beneficiaries' interest, so long as it lasts—and in this case it lasted until Brown's death.

As said in *Lewellyn* v. *Frick*, 268 U. S. 238, 251:

> "The interest of the beneficiaries is established by statutes of the states controlling the insurance and is not disputed."

The New York law governs the rights of the beneficiaries in this case; and it is well settled in New York that even where an insurance policy contains a reserved right to change the beneficiary, the property remains the property of the beneficiary, unless and until the power to change is exercised (*Wagner* v. *Thieriot*, 203 App. Div. 757, affirmed 236 N. Y. 588; *Matter of Voorhees*, 200 App. Div. 259, 262).

Therefore, the fact that the Brown policies contained provisions giving him the power to assign the policies or to change the beneficiary, did not affect the title of the wife and children to the New York Life's promise to pay, so long as the reserved power remained unexercised.

The Government errs (Brief, pp. 14, 15) in speaking of Brown's "obligation to pay the premiums for life" and "his obligation to continue to pay premiums." There was no such obligation on Brown.

He was free to abandon paying the premiums at any time he pleased.

The Government quotes some rather loose language from *Mutual Benefit Life* v. *Swett*, 222 Fed. 22, and *Mutual Reserve* v. *Cleveland Woolen Mills*, 82 Fed. 508, as to the nature of a beneficiary's interest where the policy reserves to the insured a right to change the beneficiary. But, in each of those instances, all that was *decided* was that where the husband and the wife (beneficiary) joined in an assignment of the policy, the wife was bound thereby. The beneficiary had the right to join in such an assignment and convey her interest, just as she could convey any other property rights she owned.

So long as a reserved power to change the beneficiary remains unexercised, the ownership by the beneficiary of the insurance company's promise to pay, is just as certain and as absolute as in those cases where the policies did not contain a reserved power to change the beneficiary.

2. In *Cohen* v. *Samuels*, 245 U. S. 50, cited by the Government, it was held that by the express terms of the Bankruptcy Act, a policyholder could be compelled to exercise the reserved power to change a beneficiary so as to vest in the Trustee in Bankruptcy the cash surrender value of the policies at the date of the adjudication. As the policies were taken out *after* the passage of the Bankruptcy Act, the interest of the beneficiary was, of course, subject to the paramount authority of the Bankruptcy Act. That case

rested solely upon the power of Congress under the Bankruptcy Act, and sheds no light upon the character of the title of a beneficiary to insurance moneys.

There is not, as the Government contends (Brief, p. 27), the slightest inconsistency between *Washington Central Bank* v. *Hume*, 128 U. S. 195, and *Cohen* v. *Samuels*, 245 U. S. 50, or *Burlingham* v. *Crouse*, 228 U. S. 459.

3. The fact that a State may by statute (to the provisions of which all subsequent policies are subject) provide that even policies payable to a beneficiary shall be subject to the insured's debts, does not alter the fact that *the beneficiary owns the company's promise to pay*, subject only to that statutory provision. But, it is obvious that if such a statute were passed *after* the issuance of a policy, it would be void as impairing the obligation of contracts.

4. The supposed "popular conception" that life insurance payable to a beneficiary is, nevertheless, a part of the estate which an insured "leaves" at death, even if such conception exists (which we deny), cannot determine the legal question whether such insurance is transferred from the dead to the living, so as to become constitutionally subject to an excise tax.

5. Even if it be true (which is by no means certain) that in England, since 1853, a succession duty would be imposed upon the proceeds of policies payable to a wife, that fact sheds no light whatever upon the nature of either the insured's or the beneficiary's interest in the proceeds. In England there is no

limitation upon the power to tax as between direct taxes and indirect taxes, such as exists in the United States. We concede that Congress could tax the proceeds of life insurance, payable to a beneficiary, just as completely as it is said England does. But, the difference is that in the United States such a tax must be *apportioned* in order to be valid, while no such limitation exists in England.

THIRD POINT.

The Federal Estate Tax as applied to the $160,888.21 life insurance paid by the New York Life to the widow and children is void because it is a "direct" tax and not apportioned.

I.

The Government has based its entire case on the proposition that the $200,000 life insurance received by the widow and children (and included by §402(f) in Brown's gross estate)

> "had a *close and direct relation* to the estate which he left" (Government Brief, p. 13).

Suppose it had. What then? Neither the Constitution nor the Revenue Act of 1921 says anything about "*close and direct relation.*" What is meant by such a vague phrase? To one person it might mean one thing, to another person a very different thing.

The Revenue Act levies an excise tax on the *transfer of Brown's net estate*. That does not mean that

it can tax something that is *not* a part of his estate, but only has "a close and direct relation" to it.

The whole case must turn on whether the $200,000 which the New York Life paid to the widow and children, was or was not *a part of Brown's estate.*

If it was *not* a part of his estate, then Congress could not make it so by directing its inclusion therein.

The $200,000 paid to the widow and children was a *different* thing from (1) Brown's reserved *right* to change the beneficiary, and (2) the *possible future right* in Brown *if* he paid three premiums (which he did not) to borrow against the policies or to cash them in for their surrender values (pp. 2, 3, *supra*). If we have successfully established that point, then the tax in question was not an excise levied on the *transfer of a decedent's estate* from the dead to the living, but was a "direct" tax on the $200,000 property of the widow and children; and void because not apportioned.

II.

The Revenue Act exacted a tax payment of $9,146.76 on account of the $160,888.21 life insurance. Although the Executor was required to pay the tax in the first instance, he can recover over $5,927.63 thereof from Mrs. Brown and the children; who are, in turn, personally liable for the entire $9,146.76 tax if the Executor fails to pay it.

The tax to the extent of $5,927.63 is against the widow and children. It is a *direct* tax on them solely

because they owned the New York Life's promise to pay them $200,000. They did not receive the $200,000 from Brown's estate, but from the New York Life. There was no room for an excise tax on them or in respect of any transfer from Brown to them—for the simple reason that no part of it was transferred from the dead man to the living.

The tax imposed here is not on the manufacture, consumption or use of any article; it is not imposed for the statutory privilege of inheriting money from a decedent or receiving a legacy from him, because Mrs. Brown did not receive the money from Mr. Brown. If the law had been that a decedent's entire estate should be escheated to the State upon death, thus obliterating entirely the power to transmit property at death, still Mrs. Brown would have received her insurance money just the same. This shows that the tax is not levied with respect to the transfer of a *decedent's estate*.

The fact is that the tax was imposed on Mrs. Brown and her children simply *because they owned the property*—and the privilege of *owning property* cannot be taxed except by apportionment.

The income tax cases, *Knowlton* v. *Moore*, *Flint* v. *Stone Tracy Co.*, and *Brushaber* v. *Union Pacific*, established the rule that taxes on personal property are direct taxes, and that taxes levied *because of the ownership of personal property* are also "direct" taxes (158 U. S. 601, 637; 178 U. S. 80, 82; 220 U. S. 150; 240 U. S. 19).

Mrs. Brown and her children have, since 1922, owned the promise of the New York Life to pay them $200,000 if and when Mr. Brown died. The only reason that they are required to pay $5,927.63 tax is because *they owned that promise and collected the money upon its maturity.*

If Congress levied a 10% tax in respect of every corporate bond which matured and was paid to the owner, could that be called an excise tax for the privilege of collecting the debt at maturity? Would it not be a direct tax on the bonds solely because of their ownership?

Congress has the undoubted power to tax Mrs. Brown and her children upon the $200,000 they received from the New York Life Insurance Company. But, when that money is taxed, it is taxed because of ownership and hence must be apportioned.

In *Dawson* v. *Kentucky Distilleries Co.*, 255 U. S. 288, Kentucky levied a license tax of fifty cents a gallon upon all whiskey withdrawn from bond; and called it a license tax upon "the business of manufacturing" whiskey and upon "the business of owning and storing such spirits in bonded warehouses." This Court held that the name by which the tax was described in the statute was immaterial, and that its character must be determined by its incidents. It decided that it was a property tax, because the thing really taxed was the owner's right to take possession of his own property, and that "to tax the right is to tax the value," saying (p. 294):

> "To levy a tax by reason of ownership of property is to tax the property. Compare *Thompson* v. *Kreutzer*, 112 Miss. 165; *Thompson* v. *McLeod*, 112 Miss. 383. It can not be made an occupation or license tax by calling it so. See *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 148-150; *Zonne* v. *Minneapolis Syndicate*, 220 U. S. 187; *U. S.* v. *Emery, Bird, Thayer Realty Co.*, 237 U. S. 28."

So here, the tax which Mrs. Brown and her children are made to pay is imposed upon them solely because they have taken possession of their own $200,000 which the New York Life promised to pay them in a certain contingency. The only thing which Mrs. Brown and her children have done is to receive from the New York Life the $200,000 which it had promised to pay them. To tax the act of receiving property to which one is entitled by contract, is to tax the property itself. It is for exactly that reason that the income tax cases held that a tax upon right to collect rents or interest was a direct tax upon property.

FOURTH POINT.

The $9,146.76 tax on the life insurance owned by Mrs. Brown and her children is void because it was determined in so arbitrary and capricious a manner as to violate the due process clause of the Fifth Amendment.

This Court has recognized that a statute purporting to tax may be so arbitrary and capricious as to amount to confiscation and offend the Fifth Amendment.

The 1921 Act makes both the Executors and the beneficiaries liable for the tax with respect to the life insurance owned by the beneficiaries; but, as between them, it gives to the Executors the right to recover all, or [depending on the ultimate construction of the Act] a part of, the tax from the beneficiaries.

Ultimately the beneficiaries pay the tax or most of it. But, the taxes which the beneficiaries are made to pay in respect of the property they own is not based, in any way, upon the extent of the property owned by them or any of their privileges. The amount of the tax is determined solely by the size of the *insured's estate*, with which the beneficiaries may have no concern whatever. If Mrs. Brown and her children were taxed at the "estate tax" progressive rates of the 1921 Act on the insurance which they received, they would pay about $3,000 in all. But merely because they held insurance on a well-to-do man's life, the tax is $9,146.76. In short, the Act

taxes the beneficiaries not according to any property owned or received by them, or privileges exercised, but by the amount of a third person's wealth. Is that taxation at all, or arbitrary confiscation?

On the other hand, if looked at from the standpoint of the Executors, they were required to pay $9,146.76 for an alleged transfer of Mr. Brown's estate, whereas, in truth and in fact, no part of such alleged $200,000 estate came into their hands as Executors or was in anywise subject to his debts, nor did it pass under his will. The Act has taxed the Executors for a supposed transfer of Brown's property that he did not transfer at all. The $200,000 was not transferred by the testamentary or intestate laws of New York. It neither left Mr. Brown's estate, nor did it reach the beneficiaries by virtue of any testamentary or intestate laws. The $200,000 passed solely from the New York Life to the beneficiaries as the result of a contract.

If the insurance be deemed a portion of Brown's net estate, how can Congress provide that Mrs. Brown and the children should pay a tax, not upon a legacy *received* by them, but a tax upon the *transfer of Brown's estate* and determined by the aggregate size of such estate.

Is it not purely arbitrary and confiscatory for Congress to say that A must pay a certain sum of money, determined not by A's property, acts, privileges, nor indeed anything that A receives, does or has, but determined solely by what B has? The great

power of taxation does not cover a *fiat* like that. If the power to tax includes the right to tax A on his property, privileges, etc., at a rate determined not by anything with respect to himself but with respect of B (with which standard A has no concern), then a road has been opened for Congress to avoid every constitutional limitation.

Knowlton v. *Moore*, 178 U. S. 41, 76, contains a cogent argument against the validity of the present method of determining the tax.

In *Nichols* v. *Coolidge*, 274 U. S. 531, the Federal estate tax upon the transfer of a decedent's estate was held void in so far as it attempted to include in the estate, the value of property conveyed by the testator long before the passage of the Act.

In *Blodgett* v. *Holden*, 275 U. S. 142, and *Untermyer* v. *Anderson*, 276 U. S. 440, it was held that an Act imposing an excise tax upon gifts made prior to the passage of the Act, was arbitrary and invalid under the Fifth Amendment. The point of the case is that, assuming Congress had the power to levy an excise tax on gifts, it could not tax a gift made before the passage of the Act.

Such an Act was not half so arbitrary and capricious as to tax Brown's estate, because Mrs. Brown received insurance from the New York Life, or to tax Mrs. Brown's life insurance at a rate determined by the size of Mr. Brown's estate. It might readily be that the beneficiary would receive nothing whatever from the decedent's estate, and yet would be

compelled to pay a heavy tax upon the life insurance received, simply because the decedent left a very large estate to charity, in which the beneficiary did not participate at all.

In its last analysis, this Court must determine whether Congress can, consistently with the due process clause of the Fifth Amendment, tax one person at a percentage rate, determined by some other standard, having no possible relation to the taxpayer's estate, benefits received, or privileges exercised.

WM. MARSHALL BULLITT,
Of Counsel for Plaintiffs.

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In the Supreme Court of the United States

OCTOBER TERM, 1928

No. 77

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, JAMES K. SYMMERS, GRACE B. DRAKE, et al., as Executors, etc., of Herbert W. Brown, deceased

v.

THE UNITED STATES

ON CERTIFICATE FROM THE COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

OPINION BELOW

The Court of Claims rendered no opinion and the case has not been reported.

JURISDICTION

The case has been certified pursuant to Section 3(a) of the Act of February 13, 1925, c. 229, 43 Stat. 936, 939.

THE QUESTIONS PRESENTED

The questions certified are as follows (R. 7):

"Question I. Whether the tax imposed by the final clause of section 402(f), Revenue Act of 1921,

42 Stat., 278, on life insurance policies payable in terms to beneficiaries 'other than the decedent or his estate' is a direct tax on property and void because not apportioned.'

"Question II. Whether the $9,146.76 tax imposed bears such an unreasonable relation to the subject matter of the tax as to render it void."

The statutory provisions are hereinafter set forth.

THE STATUTES INVOLVED

The revelant provisions of the Revenue Act of November 23, 1921, c. 136, 42 Stat., 227, are as follows:

> SEC. 401. That, in lieu of the tax imposed by Title IV of the Revenue Act of 1918, a tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 403) is hereby imposed upon the transfer of the net estate of every decedent dying after the passage of this Act, whether a resident or nonresident of the United States: (42 Stat. 277.)

Here follows table of percentages.

> SEC. 402. That the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated— (42 Stat. 278.)
>
> * * * * *
>
> (c) To the extent of any interest therein of which the decedent has at any time made

a transfer, or with respect to which he has at any time created a trust, in contemplation of or intended to take effect in possession or enjoyment at or after his death (whether such transfer or trust is made or created before or after the passage of this Act), except in case of a bona fide sale for a fair consideration in money or money's worth. Any transfer of a material part of his property in the nature of a final disposition or distribution thereof, made by the decedent within two years prior to his death without such a consideration, shall, unless shown to the contrary, be deemed to have been made in contemplation of death within the meaning of this title; (42 Stat. 278.)

* * * * *

(f) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life. (42 Stat. 279.)

SEC. 403. That for the purpose of the tax the value of the net estate shall be determined—

(a) In the case of a resident, by deducting from the value of the gross estate—

Here follow as deductions allowed from the gross estate, determined as provided in Section 402, certain amounts for debts, expenses, losses, charitable

gifts, etc., and a specific exemption of $50,000. (42 Stat. 279–280.)

> SEC. 406. * * * The executor shall pay the tax to the collector or deputy collector * * *. (42 Stat. 281.)
>
> SEC. 408. * * * If any part of the gross estate consists of proceeds of policies of insurance upon the life of the decedent receivable by a beneficiary other than the executor, the executor shall be entitled to recover from such beneficiary such portion of the total tax paid as the proceeds, in excess of $40,000, of such policies bear to the net estate. If there is more than one such beneficiary the executor shall be entitled to recover from such beneficiaries in the same ratio. (42 Stat. 282.)
>
> SEC. 409. * * * (b) if insurance passes under a contract executed by the decedent in favor of a specific beneficiary, and if in either case the tax in respect thereto is not paid when due, then the transferee, trustee, or beneficiary shall be personally liable for such tax, and such property, to the extent of the decedent's interest therein at the time of such transfer, or to the extent of such beneficiary's interest under such contract of insurance, shall be subject to a like lien equal to the amount of such tax. * * * (42 Stat. 283.)

STATEMENT

On September 13, 1922, the New York Life Insurance Company issued to Herbert W. Brown three policies of insurance upon his life, two for

$50,000 each and one for $100,000, and in these policies his wife, Mabel L. Brown, was named as beneficiary. (R. 4.)

On September 29, 1922, pursuant to his right under the policy to change the beneficiary, Mr. Brown made his two children, Elizabeth and Richard, beneficiaries under the $100,000 policy in place of his wife. (R. 4.) He paid the first and second annual premiums due in 1922 and 1923, respectively, amounting to $16,230. (R. 5.)

On April 10, 1924, Mr. Brown died in New York, leaving a will which was duly probated and the plaintiffs are the duly qualified executors under that will. The Chase National Bank is also guardian of Elizabeth G. Brown and Richard L. Brown, the two minor children of the deceased, and is also Committee of the property of Mabel L. Brown, the widow, who has been adjudged an incompetent. (R. 5.)

On July 30, 1924, the New York Life Insurance Company paid the amount of the three policies including accrued dividends, $100,444.10, to Mabel L. Brown's Committee, and $100,444.11 to the guardian of the minor children. (R. 5.)

For the purposes of assessing the estate tax under the Revenue Act of 1921, Mr. Brown left a gross estate, not including any part of the insurance, of $524,336.29

to which the Commissioner of Internal Revenue added the amounts paid under the policies	$200,888.21
making a total of	725,224.50
There were allowed as lawful deductions, including the $40,000 exemption allowed in Section 402(f) of the Act	139,662.93
The net estate as fixed by the Commissioner was	585,561.57

The tax assessed by the Commissioner was $21,633.69, and the amount paid by the executors was $21,691.66. (R. 6.)

In respect to $9,146.76 of the tax the executors paid it under protest upon the ground that the Commissioner had no right to include in the value of the decedent's gross estate the sum of $160,888.21 (the proceeds of the policy less the $40,000 deduction). That sum, $9,146.76, is the amount by which the Federal estate tax on Mr. Brown's estate was increased by reason of including the proceeds of the insurance companies less the $40,000 exemption. (R. 6.)

Claim for refund was duly filed by the executors, and six months having elapsed without action by the Commissioner, suit was brought in the Court of Claims.

Copies of the policies annexed to the petition which accompanies the certificate (R. 1) are set

forth at length beginning opposite page 14 of the record. They are policies of the modern type quite different from the old-fashioned straight life policy.

The first, Annex "A," names the wife as the beneficiary "with the right on the part of the insured to change the beneficiary in the manner provided in Section 6." The premiums are payable during the life of the insured. The face amount is $50,000, with so-called double indemnity for fatal accident, and disability benefits; that is, double the face of the policy will be paid if death results from external, violent, or accidental cause, and should the insured become wholly and permanently disabled before the age of sixty, the company agrees to pay to him one per cent of the face of the policy each month during his life, and also to waive the payment of premiums.

It is a participation policy. Beginning at the end of the second year the portion of divisible surplus accruing upon the policy, as apportioned by the company, shall, at the option of the insured, be either (*a*) paid in cash, or (*b*) applied toward payment of premiums, or (*c*) applied to purchase additional paid-up insurance, or (*d*) left to accumulate, at interest, with the company. Whenever the cash value of the policy equals or exceeds the net single premium at the then attained age of the insured the company agrees, upon the insured's request, to indorse the policy as a fully

paid-up policy; or, whenever the cash value shall equal the face amount of the policy the company, upon surrender of the policy, will pay in cash the face amount thereof.

After three full years' premiums have been paid, the company agrees to loan on the security of the policy amounts specified, or the insured may surrender the policy and receive the surrender value in cash or in the amount of paid-up insurance which the surrender value will purchase at that time. The surrender value is the reserve on the policy at the end of the insurance year computed on the basis of the American mortality table with interest at 3 per cent. There is also a provision, Section 5, for term insurance to cover any loan under the policy.

The insured may assign the policy, or at any time, and from time to time, change the beneficiary, provided the policy is not then assigned, by written notice to the company, accompanied by the policy, for endorsement of the change. Should any beneficiary die before the insured, the interest of such beneficiary vests in the insured. The privilege is also given the insured, prior to the age of 55 years, without medical examination, to exchange the policy for one upon any other plan of insurance issued by the company upon terms and conditions set forth. If there is no assignment of the policy the insured, or, in case the insured shall not have done so, the beneficiary after the insured's death may, by written notice to the company, make the

proceeds of the policy payable under one of several optional methods of settlement set forth in Section 8.

Finally, "the insured may, without the consent of the beneficiary, receive every benefit, exercise every right and enjoy every privilege conferred upon the insured by this policy." Except for the disability and double indemnity features, the terms of the other two policies are identical with those of the first.

SUMMARY OF ARGUMENT

The tax is an excise, not a direct tax. The only question is whether it is arbitrary and unreasonable to include in the measure of decedent's estate the proceeds of the life insurance policies.

The ownership of the policies remained in the decedent until the moment of his death. They were bought with his money and were an asset over which he had complete control while he lived and could at any moment have made payable to his estate, and if a named beneficiary should have predeceased him they would by their terms have been so payable. In bankruptcy they would have been an asset passing to the trustee.

They bore such a direct relation to his estate after death that for many years the extent to which they should be exempt from the rights of creditors has been the subject of legislative regulation.

By common understanding they are regarded as part of the estate which a man leaves when he dies,

and in England for many years have been included in the measure of death duties. Therefore, for Congress to include them was not arbitrary but was reasonable, for they bore a just and proper relation to the subject-matter of the tax.

ARGUMENT

I

THE TAX IS NOT A DIRECT TAX BUT AN EXCISE UPON THE TRANSFER OF AN ESTATE ON THE DEATH OF THE OWNER

By Section 401, the tax is imposed "upon the transfer of the net estate of every decedent dying after the passage of this Act." The value of the net estate is found by subtracting from the gross estate certain statutory deductions.

By Section 402 the value of the gross estate is determined by including the value at the time of decedent's death of all property—

(*a*) To the extent of the interest which, after his death, is subject to the payment of charges against his estate, expenses of administration and subject to distribution.

(*b*) To the extent of any interest therein of the surviving spouse such as dower, curtesy, or by virtue of a statute creating an estate in lieu thereof.

(*c*) To the extent of any interest of which the decedent has made a transfer or created a trust in contemplation of, or intended to take effect, in possession or enjoyment at or after his death.

(*d*) To the extent of the interest therein held jointly or as tenants in the entirety by the decedent and any other person.

(*e*) To the extent of any property passing under a general power of appointment exercised by the decedent by will, or by deed intended to take effect at or after his death.

(*f*) To the extent of the amount receivable by the executor as insurance, under policies taken out by the decedent upon his own life, and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries of such policies.

From the gross estate as thus determined there is deducted (Section 403)—

(1) Funeral and administration expenses, debts, losses from fire, etc., and such amounts as are allowable by the laws of the jurisdiction for the support during the settlement of the estate of those dependent upon the decedent.

(2) An amount equal to the value of the property forming a part of the gross estate of any person who died within five years prior to the death of the decedent, where such property can be identified as having been received by the decedent from such prior decedent, and where a Federal estate tax has been paid upon such property.

(3) Bequests, legacies, etc., to the United States or political subdivision thereof, or for religious, charitable, scientific, literary, or educational purposes.

(4) An exemption of $50,000.

The resultant is the "net estate," and is the amount which Congress has said shall be treated for tax purposes as the value of the estate. It is apparent that the tax as thus measured, assessed, and paid is not a tax upon the "residue" (*Edwards* v. *Slocum*, 264 U. S. 61, 62) or upon any specific property, or upon the transfer or devolution of title thereto. It is no more a tax upon the proceeds of the insurance policies than it is a tax upon the real estate, bank deposits, or bonds of the deceased. It may not even approximate the actual value of the estate. The tax is an excise or "death duty" upon the transfer of decedent's estate, like the Estate Tax under the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1096, considered in *Y. M. C. A.* v. *Davis*, 264 U. S. 47. That such a tax is an excise tax and not a direct tax is no longer open to doubt. *Knowlton* v. *Moore*, 178 U. S. 41; *New York Trust Company* v. *Eisner*, 256 U. S. 345; *Greiner* v. *Lewellyn*, 258 U. S. 384; *Y. M. C. A.* v. *Davis*, 264 U. S. 47; *Edwards* v. *Slocum*, 264 U. S. 61; *United States* v. *Woodward*, 256 U. S. 632.

The real contention of the plaintiffs is not directed against the tax but against the standard by which the tax is to be measured.

The argument of the plaintiffs may be reduced to these propositions:

(*a*) The policies of insurance were the exclusive property of the beneficiaries and formed no part of Mr. Brown's estate;

(*b*) To include them in the measure of his estate, therefore, was in effect to impose a direct tax upon them, or

(*c*) If not a direct tax upon them, the effort was to tax one person for what another person owned. Therefore the tax is so unreasonable as to be void.

II

THE POLICIES BELONGED TO MR. BROWN WHILE HE LIVED, AND THEIR PROCEEDS, AFTER HIS DEATH, HAD A CLOSE AND DIRECT RELATION TO THE ESTATE WHICH HE LEFT, RECOGNIZED BY STATUTE, BY POPULAR UNDERSTANDING, AND, FOR TAXING PURPOSES, BY HISTORIC PRECEDENT

(*a*)

The ownership of the policies, as well as all beneficial rights and interests therein, remained in the decedent until his death

These policies were not bought by Mr. Brown to indemnify a creditor, nor were they taken out upon his life by a creditor or some one else having a so-called insurable interest, who paid the premiums and thereby obtained indemnity. While all life insurance has in it the element of protection, in modern level premium life insurance the business is largely that of a savings investment and the premium is in the nature of a savings deposit.

Mutual savings banks pay to the depositor his deposit with the interest earned less the expense of management. The insurance company does the

same, the difference being merely that the savings bank undertakes to pay to each depositor the whole of his deposit with interest, while the life insurance company undertakes to pay to each member of a class the average amount, regarding the chances of life and death, so that those who do not reach the average age get more than they have deposited and those who have exceeded the average age, less than they have deposited. *Penn Mutual Life Insurance Company* v. *Lederer*, 252 U. S. 523, 531.

The old idea that life insurance was solely for the benefit of those who survived the insured, has wholly disappeared. The policies which we have here, secured for Mr. Brown the moment he bought them substantial benefits which remained his absolutely and of which he could not be deprived while he lived. One of them assured him an income for life, if he became disabled, without further payment of premium. Each of them became available as collateral for loans and provided a cash surrender value. The moment he paid the first premium he acquired an asset which he had the power to do with as he pleased during life and dispose of as he chose at death.

He also assumed an obligation. Insurance contracts of this kind are not contracts for a year with the privilege of renewal from year to year, but are "entire contracts for life" subject to forfeiture, of course, by failure to perform the conditions. *McMaster* v. *New York Life Insurance Company*, 183

U. S. 25, 35. The premiums constitute an annuity the whole of which is the consideration for the entire assurance for life. *New York Life Ins. Co.* v. *Statham*, 93 U. S. 24.

The obligation of the insured to pay the premiums for life is the consideration for the promise of the company to pay the face of the policy at death. Indeed the reserve at the end of any year is the difference between the present values at that time of these reciprocal contracts. The fact that Mr. Brown died in the early years of the policy when the cash value was negligible, instead of later, when those values were large and approached the face value, does not alter the principle. The payment of the first premium and his obligation to continue to pay premiums entitled him at once to all the contractual benefits under the policies. The policies were his, and his alone, and were part of his estate. To the extent of their cash surrender value they would have passed to his trustee in bankruptcy. *Burlingham* v. *Crouse*, 228 U. S. 459; *Cohen* v. *Samuels*, 245 U. S. 50.

By the express terms of the policies the right to participate in the surplus and receive the dividends; to borrow; to surrender; to convert into other forms of insurance; to assign; to change the beneficiaries; in short to "receive every benefit, exercise every right and enjoy every privilege conferred upon the insured by this policy" belonged to him and to him alone, and could be received, exer-

cised, and enjoyed without the consent of the beneficiaries. Upon his death those rights ceased, his obligations ended, the policy "matured."

What passed to the beneficiaries was what he had bought by performing his policy obligations and by failing to exercise his policy privileges. He had, during life, subtracted from his means money which, when he died, was to "reappear in the form of a beneficial interest accruing or arising on his death." (See *Lethbridge* v. *Attorney General*, (1907) A. C. 19, 23.)

Such being the fact it only tends to confuse the question here involved to argue whether the beneficiary's interest was "vested," or "vested subject to be divested," or "contingent," or a "mere expectancy." Whether it was like an estate to last until "A" comes from Rome, or unless "A" comes from Rome, or if "A" comes from Rome, is unimportant. It is plain that the beneficiaries could exercise no control, enjoy no right, derive no benefit from the policies until Mr. Brown should die, and then their rights and benefits would be only those which he chose to leave to them.

Under such policies it seems to be well settled that the beneficiary has no right or interest properly described as "vested," but merely an expectancy.

In *Mutual Benefit Life Insurance Company* v. *Swett*, 222 Fed. 200 (C. C. A. 6th Cir.), the court after stating that the rule was well settled that un-

der an ordinary policy of life insurance in which there was no reservation of a right to change the beneficiary the beneficiary acquired the moment the policy was issued a vested right which could not be affected by any act of the insured, said at page 204:

> If, however, by the terms of the policy itself there is reserved to the insured the right, without the consent of the beneficiary, to change the appointee with the assent of the insurer, the beneficiary acquires only an expectancy and not a vested interest during the life of the insured. * * *
>
> The right so reserved rests upon the terms of the contract, and is the same as that conferred on the insured by the certificate, charter, or by-laws of a mutual or benefit association, when insurance is effected in such an organization. As the policy to Swett stipulated that he might, on his written request of the company for its appropriate indorsement on the policy, change the beneficiary, his wife did not acquire a permanent or vested interest in it. The existence of such an interest during her husband's lifetime was made impossible by the control over the contract of insurance given to him, independent of her will. Her right was inchoate, a mere expectancy during his lifetime, dependent on the will and pleasure of her husband as holder of the policy, and could not vest until his death happened with the policy unchanged. His control over the policy was, subject to its items, as complete as if he him-

self had been the beneficiary. *Denver Life Ins. Co.* v. *Crane*, 19 Colo. App. 191, 200, 73 Pac. 875. The wife had no vested interest which she could assign until the death of her husband—no assignable or transferable interest in the policy until some right of action on it accrued in her favor. May on Ins., Sec. 399 F; *Sabin* v. *Phinney*, 134 N. Y. 423, 428, 31 N. E. 1087, 30 Am. St. Rep. 681.

In *Reid* v. *Barborak*, 272 Fed. 99 (C. C. A. 4th Cir.), the court said at page 101:

> It is true that one named as beneficiary has no vested interest and is not entitled to notice of change; that the right to change a beneficiary is a property right of the assured, which in the case of insolvency the court can require him to exercise in favor of his creditors.

Citing *Cohen* v. *Samuels*, 245 U. S. 50.

In *Cohen* v. *Samuels*, 245 U. S. 50, this Court held that a policy of insurance held by a bankrupt, which had a cash surrender value at the time of the adjudication, became an asset in the trustee even when the policy was payable to some one other than the bankrupt, his estate, or personal representatives, if the bankrupt has reserved absolute power to change the beneficiary. Referring to the fact that the policies were not payable to the bankrupt or his estate, the Court said, page 53:

> It is true the policies in question here are not so payable, but they can be or could have been so payable at his own will and by simple

declaration. Under such conditions to hold that there was nothing of property to vest in a trustee would be to make an insurance policy a shelter for valuable assets and, it might be, a refuge for fraud.

In *Mutual Reserve Fund Life Association* v. *Cleveland Wooden Mills*, 82 Fed. 508 (C. C. A. 6th Cir.), the court had under consideration a policy issued by a company conducting an insurance business on the cooperative or assessment plan, and under the statute of New York, where the Association was organized, any member had the right at any time, with the consent of the Association, to make a change in the payee or beneficiary without the consent of the latter. Circuit Judge Lurton, writing for the court, said at page 519:

> Mrs. Parker had no vested interest in this policy, and the assured, under this provision of the law governing this contract, had the right to change the beneficiary. There was no contract between the member and payee by which any interest was vested in Mrs. Parker. The original designation of Mrs. Parker as the beneficiary was in the nature of an inchoate or unexecuted gift, and left the member free, under the provision of the law above quoted, to change the payee at his pleasure, with the consent of the company. That Mrs. Parker paid some of the assessments is not material, as it is not shown that she did so with her separate estate, or under any contract by which she was to acquire a vested right.

See also *New York Life Insurance Company* v. *Cook*, 237 Mich. 303; *Schoenholz* v. *N. Y. Life Ins. Co.*, 234 N. Y. 24; *May on Insurance*, Sec. 399 (m); *Cooley's Briefs on Law of Insurance*, page 3755; *Joyce on Insurance*, Sec. 731.

In *Barbour* v. *Equitable Life Assurance Society*, 174 App. Div. 759 (affirmed without opinion, 225 N. Y. 675), the court said, at page 761:

> The plaintiff was the beneficiary named in the policy, but of course had no substantial right in the same until after the death of her husband while the policy was in force; up to his death, and while in possession of the policy, Mr. Barbour had an absolute right to change his beneficiary, and the plaintiff was not a party to the contract in any material sense while her husband was alive and prepared to act.

Even where there is no right to change the beneficiary, his rights are not vested so absolutely that they can not be divested, and they are subject to the other terms of the contract.

In *Schuberth* v. *Credential Insurance Company*, 86 Pa. Superior Court 80, the court said, at page 82:

> Appellant argues that it is useless to say that she has a vested interest if he can borrow money against the policy; that the right to borrow is in reality a right to exhaust the benefits of the policy presently. There is force in this contention but the answer is that the parties had made their contract and

> the interest in the beneficiary, although vested, is subject to the provisions of the contract. The contract expressly declares that the insured may borrow.

In *Smith* v. *Metropolitan Life Insurance Company*, 222 Pa. 226, it appeared that one Gordon took out five policies on his own life. No beneficiary or person to whom the insurance should be paid on the death of the insured was named in any of the policies, but from matter contained in the applications for three of them, and by concessions at the trial, the trial court treated all the policies as though Gordon's wife had been named as the beneficiary. The wife died first, and thereafter the husband, by written order on a blank furnished by the company, appointed his daughter as the beneficiary. She brought suit, and on the trial was nonsuited on the ground that the interest in the policies had "vested" in the wife and at her death passed to her administrator as part of her estate. In reversing the judgment the Supreme Court of Pennsylvania said, at page 229:

> The naming of a beneficiary to whom payment is to be made is a gift of a benefit in future, but is contingent on the circumstances. Thus it carries with it no obligation to the beneficiary that the donor will keep the policy alive by continuing to pay the premiums. That is contingent on his doing so voluntarily. And the nature of the thing given would seem to imply that the beneficiary must survive the insured. Thus in the pres-

> ent case the gift is equivalent to a provision that when the husband dies, having kept the policy alive, the wife shall be entitled to the money. But the intent is to provide for her, not for any other, and if she has died first, the expressed intent is incapable of fulfillment and we are not at liberty to supply a further intent which the donor did not indicate. He might have done so by naming her executor, or administrator, or children, at his own choice, but as he did not do so we are not authorized to make a choice for him. The natural presumption is that he did not desire such result, nor intend to continue to pay premiums for the benefit of any other person.

It would, of course, be idle to say that there are not cases containing language to the contrary; but we are not concerned so much with matters of terminology as we are with matters of substance. The rights of the beneficiaries under policies involved in this case are plain, whatever term may be used in describing them. It is, of course, beyond dispute that upon Mr. Brown's death the right of the beneficiaries to the proceeds vested subject to the rights of creditors hereinafter discussed. Up to that time they had nothing of present value which could be assigned; which would serve as security for a loan, or which at the death of the beneficiary would pass to the heirs or personal representatives.

The policies were at all times subject to the right of the assured to surrender them for cash or borrow from the company upon them, and if they had been in force long enough, borrowing might have rendered them practically valueless, for if Mr. Brown had availed himself of his right to borrow from the company *the amount of the loans would have been payable out of the policies and not out of funds of his estate in the hands of his executors.* *Wagner* v. *Thieriot*, 203 App. Div. 757, affirmed 236 N. Y. 588 on opinion below.

Perhaps we have given more space to this question than is necessary. Plaintiffs, however, seem to feel, correctly as we think, that their whole case depends upon establishing this point. Their principal reliance is upon *Tyler* v. *Treasurer and Receiver General*, 226 Mass. 306, and *Central Bank of Washington* v. *Hume*, 128 U. S. 195. In the former case the court was called upon to decide whether the proceeds of certain life insurance policies were, under the Massachusetts succession tax, imposed by St. 1912, c. 678, Section 1, as amended by St. 1913, c. 498, property "which shall pass by * * * gift * * * made or intended to take effect in possession or enjoyment after the death of the grantor."

After a general discussion of the relation between the insured and the beneficiary, under life insurance policies, the conclusion was that "such a relation does not by fair intendment come within

the descriptive words of the statute." That conclusion was strengthened by reference to the principle that "tax laws are not to be stretched beyond their reasonable meaning, but rather in cases of doubt are to be construed with some strictness." "If an alleged right to tax does not fall within the words of the governing statute, it does not exist." The court added, page 310—

> This conclusion is confirmed by the practical construction put upon the law by those charged with the enforcement of the law through many years, a circumstance sometimes entitled to considerable weight.

With the conclusion of the court we have no quarrel. It does not by any means carry with it the inference, however, that the court would have found anything objectionable in the statute had it, in so many words, said that the proceeds of life insurance policies should be included in measuring the estate.

The report of the case does not describe the policies beyond saying (p. 309)—

> None of the policies in the cases at bar are commercial contracts which bear any earmarks of being designed to avoid the operation of the tax law. On the contrary, they are well-recognized forms of insurance which have been in common use for a long time.

Chief Justice Rugg's discussion of the nature of insurance policies is based upon decisions of the Massachusetts courts, and upon *Central Bank of*

Washington v. *Hume*, 128 U. S. 195, where it is said at page 206:

> It is indeed the general rule that a policy, and the money to become due under it, belong, the moment it is issued, to the person or persons named in it as the beneficiary or beneficiaries.

That, of course, is not an accurate statement of the law today as applied to policies such as we are now considering. *Burlingham* v. *Crouse*, 228 U. S. 459; *Cohen* v. *Samuels*, 245 U. S. 50.

The case of *Central Bank of Washington* v. *Hume*, 128 U. S. 195, has been frequently cited, sometimes without due regard to the facts involved. The question decided is set forth in the syllabus as follows:

> The payment of premiums to a life insurance company by a married man residing in the District of Columbia, who is insolvent at the times of the payments, in order to effect and keep alive a policy of insurance upon his own life, made by his wife for the benefit of herself and their children, is not necessarily a fraudulent transfer of his property with intent to hinder, delay and defraud creditors within the meaning of 13 Eliz. c. 5; and in the absence of specific circumstances showing a fraudulent intent, his creditors, after his decease, will have no interest in the policy.

Mr. Hume having been insolvent at the time the insurance was effected, and having paid the premi-

ums himself, it was urged that the policies were within the provisions of the statute of Elizabeth and inured to the benefit of his creditors, as equivalent to transfers of property with intent to hinder, delay and defraud.

It does not appear that the policies contained any power to change the beneficiaries or other provisions similar to those in the policies we are now considering. One of them was for the " sole use and benefit of his wife, Annie Graham Hume and his children, payment to be made to them, their heirs, executors, or assigns * * *" (p. 195.) Some were payable to the wife if living, but otherwise to Hume's legal representatives. One was payable to "the said insured, Annie G. Hume, for her sole use, her executors, administrators, or assigns." (p. 196.) One was payable to Annie G. Hume and her children by him, or their legal representatives." (p. 197.)

The court treated the contracts as having been *made by the wife herself upon the insurable interest of herself and her children in her husband's life.* After discussing the object of the statute of Elizabeth, and the nature of insurable interests, the Chief Justice said (p. 206):

> We think it can not be doubted that in the instance of contracts of insurance *with a wife or children*, or both, upon their insurable interest in the life of the husband or father, the latter, while they are living, can exercise no power of disposition over the

> same without their consent, * * *. (Italics supplied.)

Then follows the sentence upon which so much stress is laid (p. 206):

> It is indeed the general rule that a policy, and the money to become due under it, belong, the moment it is issued, to the person or persons named in it as the beneficiary or beneficiaries, and that there is no power in the person procuring the insurance by any act of his, by deed or by will, to transfer to any other person the interest of the person named.

It is apparent that this language was used with reference to the policies then under consideration. In so far as it holds that a policy, and the money to become due under it, belongs the moment it is issued to the beneficiary, and that there is no power in the person procuring the insurance to transfer to any other person the interest of the person named, it has not, and can not have any application to such policies as are here involved. That would of course be inconsistent with the later decisions of this Court in *Burlingham* v. *Crouse*, 228 U. S. 459, and *Cohen* v. *Samuels*, 245 U. S. 50.

This Court has distinguished the case in *Royal Arcanum* v. *Behrend*, 247 U. S. 394, in which it was said (p. 398):

> This court held in *Washington Central Bank* v. *Hume*, 128 U. S. 195, 206, that under the ordinary policy of life insurance, when no right is reserved to surrender the policy

> or to change beneficiaries, the beneficiary named therein acquires, at the moment it is issued, a vested right which can not be affected by any act of the insured subsequent to the execution of the policy. The rule there declared was deemed by the Court of Appeals to control the case at bar. But it was not applicable; because the contract sued on was a benefit certificate of a fraternal benefit association, not an ordinary policy of life insurance; and also because the benefit certificate on its face reserves the right to change beneficiaries.

The policies considered in the *Hume* case were issued between 1872 and 1881, and the case was decided in 1888.

It was well said in *Schade* v. *Western Union Life Insurance Company*, 125 Wash. 200, 205:

> Until the last two or three decades, life insurance policies did not contain any express reservation of power in the insured with reference to a change of the beneficiary, and in all of the earlier cases if the courts in construing policies concluded there was conferred upon the beneficiary named in the policy what was termed a vested interest, because of any rule of substantive law or public policy, or simply by judicial construction of the particular contract under consideration, those decisions can be of little purpose here, where, by the terms of the policies, the insured was given unlimited power and control so far as the rights of the beneficiary are concerned.

It is safe to say that no life insurance company would dream of instructing its agents when selling policies to represent to prospects that such policies as these belonged, the moment they were issued, to the person named as beneficiary whose rights could not thereafter be affected by any act of the insured.

(*b*)

The Relation to the Estate of a Decedent of the Proceeds of Insurance upon his Life

In New York, since 1840, by statutory provision, insurance on a husband's life for the benefit of his wife, where the annual premiums paid from the husband's property exceeded a certain sum, $500 at the present time, that portion of the insurance money purchased by the excess of premiums has been liable for the husband's debts if his estate was insolvent. Domestic Relations Law, c. 14, Consolidated Laws, Section 52, derived through various revisions from c. 80 of the Laws of 1840; *Kittel* v. *Domeyer*, 175 N. Y. 205; *Guardian Trust Company* v. *Straus*, 139 App. Div. 884, affirmed without opinion, 201 N. Y. 546. The latter case held that it was the duty of an executor to reduce this asset to possession. Statutes of this kind are exemption statutes. *Elsom* v. *Gadd*, 93 Wash. 603.

In *Kittel* v. *Domeyer*, 175 N. Y. 205, 212, in discussing the New York statute it was held that the wife's right did not rest upon the contract but "upon a legislative grant, by way of exemption

from the claims of creditors, of an insurance fund, created by the husband's annual appropriation, or investment of his moneys. * * * The right of the State is clear to change and to regulate the exemption, before the insurance fund, which the husband accumulates during his life, reaches the wife."

In Connecticut, ever since 1850, there have been statutory provisions making the amount of the premiums in excess of a given amount, together with interest thereon, chargeable with the husband's debts. In *Bartram* v. *Hopkins*, 71 Conn. 505, the court, after tracing the statute back to its source in a law passed in 1850, prior to which time the property rights of married women were substantially those conferred by the common law, by which a husband, whether solvent or insolvent, could not make a gift to his wife of personal property which would be valid against him or his creditors, said, at page 518:

> In both acts, for one thing, we think the legislature intended to limit the amount which a husband could divert from his creditors in this particular form of gift, and to say that all given beyond the statutory amount should be liable to his creditors.

The conclusion was that the plaintiff did not have to show that the excess premiums were paid in fraud, actual or constructive, of creditors.

In *Coates* v. *Worthy*, 72 Miss. 575, the court discussed a statute which provided that insurance to

the amount of $5,000, payable to the executors or administrators, should inure to the heirs or legatees of the decedent free from liability for his debts, but if he was otherwise insured for the benefit of heirs or legatees at the time of his death the sum collected should be deducted from the $5,000 and the excess only should be exempt.

There are numerous statutory provisions in the different jurisdictions exempting proceeds of insurance upon the life of a debtor from payment of his debts, sometimes with limitations as to the amount or as to the beneficiary entitled to the exemption. See 25 *Corpus Juris*, p. 72, title "Exemptions." But it is unnecessary to discuss them. The details of these various statutory provisions and of the cases arising under them are not important. The important thing is that for years, and ever since life insurance attained recognition as an economic feature of every-day life, its relation to a man's estate has been deemed generally a proper subject for legislative consideration, definition, and regulation. The proceeds of a policy have been treated as a "fund" which the insured "accumulates during his life," and the State has a clear right to regulate the exemption from claims of creditors to which it shall be entitled. *Kittel* v. *Domeyer*, 175 N. Y. 205.

This Court held in *Bank of Minden* v. *Clement*, 256 U. S. 126, that a life-insurance policy payable to the executors, administrators, or assigns of the insured was his property, subject to the claims of

his creditors, and that a State law exempting the avails of such policies from his debts was invalid as applied to a debt antedating the law, and to policies antedating it though later than the note evidencing the debt. There is very little practical difference between such a policy and one under which the insured can change the beneficiary from his estate to another and back again at will and as often as he pleases.

(c)

The popular conception of Life Insurance as part of a Decedent's Estate

It is safe to say that the amount of life insurance which one carries is almost universally regarded in common understanding and popular speech as part of the estate which he "leaves" when he dies. In the case of men of large wealth the insurance may be, and probably in most cases is, so small proportionately that it is not noticed. In the case of many men it is about all they leave.

In the case at bar the gross estate exclusive of insurance was about two and one-half times the life insurance. Probably no man ever insured his life in favor of those who were the natural objects of his solicitude, without at the same time registering the thought that then and there he had acquired an estate, an asset while he lived, and something which he could leave to his family upon his death.

Under the modern form of policy, where the insured has complete control with the right to change of beneficiary at will, and with the right to exercise the various options which the policies provide, this popular conception is in accord with the realties of the situation. In popular thought it is as much a part of a man's estate as anything he possesses. He can pledge it, spend it, or lose it while he lives, and by will can provide for its disposition afterwards.

No man making inventory of his possessions for the purpose of drawing his will would fail to take account of his life insurance, and the relation of the insurance to his other property might, and in many cases undoubtedly does, control the disposition of the other property. If the average man includes his life insurance in measuring his estate for the purpose of making testamentary disposition thereof, what reason is there why Congress should not apply the same measure for purposes of taxation? It can not be arbitrary, capricious, unreasonable, and confiscatory for Congress to reason as does the ordinary man in respect to the same question.

On December 10, 1914, Honorable A. Barton Hepburn delivered an address at the annual meeting of the Association of Life Insurance Presidents in the City of New York, upon "the relation of life insurance to the credit fabric of business." In the course of the address, speaking of the man who carried life insurance, he said:

> Anxiety and worry yield to the comforting conviction, day by day, that his insurance will enable his estate to make full restitution to those who have given him their confidence and credit, or better still, that his insurance will care for and maintain his loved ones when his supporting hand no longer avails.

(*d*)

Historically the Proceeds of Life Insurance Policies have for many years been included in the Measure of Death Duties

In *Knowlton* v. *Moore*, 178 U. S. 41, this Court sustained the legacy tax under the War Revenue Act of 1898, and afterwards in *New York Trust Company* v. *Eisner*, 256 U. S. 345, the estate tax under the Act of September 8, 1916, c. 463, 39 Stat. 756, 777. In each case the statute was assailed as imposing a direct tax without apportionment, and in each case the decision was based largely upon the practical and historical ground that such taxes had always been regarded as duties or excises and not by attempting to make scientific distinctions. 256 U. S. 349.

In *Knowlton* v. *Moore* the Court pointed out that death duties in one form or another had for many years, in England and other countries, been regarded not as direct taxes but as excises. After referring to the fact that such taxes were known to the Roman law and the ancient law of the Continent of Europe, the Court said (178 U. S. 48):

> The term "Death Duties," by which inheritance and legacy taxes, in whatever form imposed, are described in England, indicates the generic nature of such taxes.

The Court quoted from Hanson's Death Duties, showing the development of such forms of taxation from the probate duty in 1694 down to the Finance Act of 1894. In 1780 the probate duty was supplemented by what came to be known as a legacy tax, and in 1853 the probate duty tax and the legacy tax were supplemented by a tax known as the succession duty. As showing the nature of the Succession Duty the Court quoted from Hanson, page 50 as follows:

> Succession duty is a tax placed on the gratuitous acquisition of property which passes on the death of any person, by means of a transfer (called either a disposition or a devolution) from one person (called the predecessor) to another person (called the successor).

In a note to Section 2 of that Act, Hanson, after quoting decisions, says (p. 629):

> It follows from these decisions that a gratuitous assignment *inter vivos* by the owner of a policy of assurance effected on his own life, creates a succession between him and his assignee in respect of the moneys which are received after his death by virtue of the policy, and it is the constant practice to pay duty under such circumstances (see opinion of Sir Wm. Atherton and Sir Roundell

> Palmer, *Re Earl of Aberdeen*, 11 March, 1862, MS.), and it makes no difference in such a case that he does not expressly bind himself to pay the premiums necessary for keeping the policy on foot, if in point of fact he actually does pay them, for it is evident that under such circumstances the whole of the assurance money is derived from his gift. If, however, the premiums are paid by the assignee, no succession duty is payable (*Ld. Adv.* v. *Fleming*, 1897 A. C. 145; *Ld. Adv.* v. *Robertson*, 22 S. S. C. 4th ser. 568).

The Succession Duty Act of 1853 was followed by the Finance Act of 1894, creating what was called an estate duty. That Act provided in Section 2 (Hanson, page 82) that "property passing on the death of the deceased shall be deemed to include," among other things, any annuity or other interest purchased or provided by the deceased either by himself alone, or in concert, or by arrangement with any other person to the extent of the beneficial interest accruing or arising by survivorship or otherwise at the death of the deceased. In a note to this section Hanson says, page 105:

> Policies of assurance included in a marriage settlement come within this sub-section; for such a policy is an interest provided by the deceased, generally by arrangement with some other person, whereby a beneficial interest arises on the death of the deceased.

Among other cases which he cites is *Lethbridge* v. *Attorney General* (1907) A. C. 19, in which Lord Chancellor Loreburn said (p. 23):

> The general purpose of this sub-section is to prevent a man escaping estate duty by substracting from his means, during life, moneys or money's worth, which, when he dies, are to reappear in the form of a beneficial interest accruing or arising on his death.

With respect to the policies which are included within the measure of the Act, Hanson says (p. 4):

> Policies of assurance on the life of the deceased, which he has given away in his lifetime, but the premiums on which he has continued to pay. For instance, the deceased has insured his life and given the policy to his wife, but has himself paid the premiums; estate duty is payable on the policy moneys. The same result would follow if the policy were taken out in the name of the wife. But if he only pays part of the premiums, only a proportionate amount of the policy moneys will be chargeable with duty.

It appears, therefore, that in England, ever since 1853, the proceeds of life insurance policies have been regarded as property to be included in the measure of the tax under the statutes which this Court regarded as historic precedents for classifying legacy and estate taxes not as direct taxes but as duties or excises grouped under the generic term "death duties."

In *Attorney General* v. *Pearson* [1924], 2 K. B. 375, the court had under consideration a tax case under the Finance Act of 1894. The decedent had settled certain policies of insurance on his life in

trust for himself until marriage and thereafter in moneys payable under the policies in trust to pay the income to his wife for life, and after the decease of his wife in trust for the children, and if there should be no children of the marriage he should acquire an interest in the fund in trust for the settlor absolutely. The case seems to have turned upon the question whether the deceased had an interest within the meaning of the Act in the moneys which were to become payable under the policies. Mr. Justice Rowlatt, in deciding the case, said, page 388:

> I can not see that the deceased never had an interest in this property. On the contrary I think he had an interest in it. He had an interest in the policies before he settled them. Moreover after he settled them he had an interest in the benefit which was going to accrue or arise from them on his death, though it may have been a remote interest which he never could enjoy in possession. He had an interest during all his married life contingently upon the failure of the trusts in favor of his wife and children. If his wife and his children had predeceased him the legal position would have altered, but his interest would then have become a very proximate and extremely valuable interest, and he would have died worth the capital value of the insurance money.
>
> That being so, my judgment must be for the Crown with costs.

III

AS THE PROCEEDS OF THE POLICIES BEAR A JUST AND REASONABLE RELATION TO THE SUBJECT MATTER OF THE TAX, IT WAS WITHIN THE POWER OF CONGRESS TO INCLUDE THEM IN ITS MEASURE

In *Flint* v. *Stone Tracy Company*, 220 U. S. 107, sustaining the corporation excise tax of 1909, measured by income, after an exhaustive review of the subject this Court held that the only constitutional restriction upon the authority of Congress to fix the measure of an excise tax is that the measure must not be arbitrary but must be based upon a reasonable ground and bear a just and proper relation to the subject matter of the tax. About the constitutionality of an estate tax like the one here there can be no question, since *New York Trust Company* v. *Eisner*, 256 U. S. 345. The sole question is whether it is arbitrary and unreasonable to include in the measure of the tax the policy proceeds.

We have seen that these policies and all rights under them belonged to the deceased during his life to do as he pleased and in bankruptcy would have been available to his creditors; that if he died insolvent, to a considerable extent the proceeds would have been liable for his debts under the laws of the State where they were issued and where he died; that in many States the extent and nature of the exemption to which they would have been entitled has been deemed a proper subject for legislative regulation; that by common understanding

and in popular speech they are regarded as part of a man's estate, and that for many years they have been treated as part of the estate under statutes imposing taxes of this same generic group. This Court said in *Nicol* v. *Ames*, 173 U. S. 509, at page 515:

> In deciding upon the validity of a tax with reference to these requirements, no microscopic examination as to the purely economic or theoretical nature of the tax should be indulged in for the purpose of placing it in a category which would invalidate the tax. As a mere abstract, scientific or economical problem, a particular tax might possibly be regarded as a direct tax, when as a practical matter pertaining to the actual operation of the tax it might quite plainly appear to be indirect. Under such circumstances, and while varying and disputable theories might be indulged as to the real nature of the tax, a court would not be justified, for the purpose of invalidating the tax, in placing it in a class different from that to which its practical results would consign it. Taxation is eminently practical, and is in fact brought to every man's door, and for the purpose of deciding upon its validity a tax should be regarded in its actual, practical results, rather than with reference to those theoretical or abstract ideas whose correctness is the subject of dispute and contradiction among those who are experts in the science of political economy.

The same principle should apply here. Resort should not be had to abstruse and subtle distinctions

and microscopic examination of a theoretical nature in order to curb and cripple the great taxing power of Congress. This statute tries to bring within its scope every conceivable phase of modern ingenuity in creating and passing estates. Proceeds of insurance policies pass after the death of the decedent in a manner not substantially different from property which passes by will, inheritance, or intestacy, and Congress has deemed it proper to subject it to the same burden of taxation. This is not the use of the taxing power for an ulterior purpose, as in the *Child Labor Tax Case*, 259 U. S. 20, and the like. It is merely carrying out logically the collection of sources of revenue made available under *Knowlton* v. *Moore*, 178 U. S. 41, and *New York Trust Company* v. *Eisner*, 256 U. S. 345.

In *Matter of Schmidlapp*, 236 N. Y. 278, a case under the State transfer tax law, the court had under consideration a deed of trust which provided that the income should be paid to the grantor during his lifetime up to a certain date, after which or prior to his death, the income was to be paid to his sons during their lives with the right to them to dispose of the principal by appointment, but reserving to the grantor the right to direct and control investments during the continuance of the trusts and to modify, alter, or revoke in whole or in part the indentures. The question was, when the gift to the sons took effect for purposes of taxation? In an opinion by Chief Judge Cardozo the court held that the distinction between a gift which clothes

the donee with a right of present enjoyment, though subject to revocation at the will of the donor, and one where the donor reserves to himself not only the power to revoke but also enjoyment during life, so that no beneficial right enforceable against him exists until his death, is that in the one class of cases the law in force at the delivery of the deed and in the other the law in force at death is the measure of the right to tax. In the course of his opinion the Chief Judge said, page 284:

> The statute is assailed as a denial of "due process." The assault, we think, must fail. A gift by deed of trust to take effect in enjoyment upon the death of the donor, with the reservation of intermediate use, and with complete power of revocation, approaches so nearly to a gift by will that the legislature may declare their substantial identity for the purpose of taxation. (*Matter of Dows*, 167 N. Y. 227; *Orr* v. *Gilman*, 183 U. S. 278; *Matter of Delano*, 176 N. Y. 486; *Chandler* v. *Kelsey*, 205 U. S. 466.) The execution of such a deed is ineffective to clothe the donee with any right enforcible against the resistance either of the donor himself or of his personal representatives until the deed has been followed by death and the election to leave it unrevoked. Until then, any right that is acquired is imperfect and inchoate. The operative events that fill out the measure or content of a right are in a very real sense the events that fix the moment of its creation.

So in the present case. The naming of a beneficiary, with "complete power of revocation" reserved, was "ineffective" to clothe the beneficiary with any enforceable right until the death of the insured with the election to leave the designation unrevoked. Death was the operative event that filled out the measure of the right and fixed the moment of its creation. It approached so near a transfer by will or intestacy that Congress could rightfully declare their substantial identity for purposes of taxation.

If in order to support the tax it is necessary to rely upon a technical transfer from the assured to the beneficiary, it is plain that there was a transfer within the meaning of the statute. While it may be true that the beneficiaries got their money not from the executors but from the insurance company, it is also true that the interest which the assured had in the policies up to the moment of his death then ceased. If he had lived until the reserve equaled the face of the policies, they would then have matured and been paid to him. Upon his death the beneficiaries succeeded to that right, for his death matured the policy.

Nothing is paid over by the insurance company, whether to executors or directly to a named beneficiary, except the "fund" which he has created by "annual appropriation, or investment, of his moneys," *Kittel* v. *Domeyer*, 175 N. Y. 205, 212, *supra*, the fund which, if paid to the executors, would concededly be subject to the tax. It was his

money which brought the fund into being; his money which continued its life; and his death which caused that money to reappear in the form of a beneficial interest for them instead of for him. The fact that in the present case the amounts payable to the beneficiaries were much larger than the cash surrender value of the policies does not alter the principle. If instead of having been in force two years they had been in force many years, the difference might not have been great.

It seems to be conceded that proceeds of policies payable to the decedent or his estate are subject to the tax, but the difference between a bequest of the proceeds of a policy payable to the estate of the decedent, and the naming of a beneficiary in a policy of this kind is theoretical and unsubstantial. Why is it not reasonable to apply the same rule of taxation to both? As the proceeds of the policies bear a just and reasonable relation to the subject matter of the tax, it was within the power of Congress to include them in its measure. *Flint* v. *Stone Tracy Company*, 220 U. S. 107; *Greiner* v. *Lewellyn*, 258 U. S. 384.

IV

THE QUESTIONS RELATING TO THE MODE PROVIDED FOR THE COLLECTION OF A PORTION OF THE TAX BY THE EXECUTORS FROM THE BENEFICIARIES ARE NOT NOW BEFORE THE COURT

The questions relating to the mode provided for the collection by the executors from the beneficiaries of a portion of the tax paid need not be consid-

ered now, for they are not properly before the Court. The statute requires the executors to pay the tax, and they have paid it. Sections 408 and 409 of the statute give them a right of action against the beneficiaries to recover such portion of the total tax paid as the proceeds of the policies in excess of $40,000 bear to the net estate. The plaintiffs claim that this formula results in what they conceive to be inequality.

If we are right in our conclusion that the proceeds of the policies may properly be included in the gross estate in measuring the tax to be assessed upon the transfer of the net estate, then the executors could not complain if they were required to pay it all without any right of reimbursement. Of course, the testator could have directed the executors to pay the tax out of the residuary estate without attempting to recover any part. Should the executors sue a beneficiary to recover any portion of the tax the respective rights of the parties would then be determined.

As the executors paid the contested charge out of property which actually passed by death, only their rights are here involved. *Nichols* v. *Coolidge*, 274 U. S. 531, 541. It may be, as suggested in *Lewellyn* v. *Frick*, 268 U. S. 238, 251, that a serious question must be answered before the beneficiaries can be made to pay a portion of the tax, but we are not concerned with that question here. The only question is whether it was competent for Congress to in-

clude in the measure of the decedent's estate the proceeds of these policies.

If the decedent had made the policies payable to his estate, so that the proceeds would have passed by intestacy or by will, it is obvious that the amount of the estate tax would have diminished the amount receivable by the legatees or by the wife and next of kin. That being so it is hard to see what injustice there is in requiring the beneficiaries to return that which would have been deducted before it came to them, if the property had gone through the hands of the executor. If the beneficiaries are put in the position of intestate successors, then as to them the tax is not imposed upon them but precedes them, and the fact that they may receive less or different sums because of the statute does not concern the United States. *New York Trust Company* v. *Eisner*, 256 U. S. 345, 349.

CONCLUSION

Both questions certified should be answered in the negative.

WILLIAM D. MITCHELL,
Solicitor General.

ALFRED A. WHEAT,
Special Assistant to the Attorney General.

NOVEMBER, 1928.

Office Supreme Court, U. S.
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IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1928.

No. 77

THE CHASE NATIONAL BANK

vs.

THE UNITED STATES.

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIÆ AND BRIEF.

L. L. HAMBY.

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IN THE

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THE CHASE NATIONAL BANK

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MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIÆ AND BRIEF.

The undersigned represents to the court that he is counsel for the plaintiffs in the case of Martha A. Guettel, et al. *vs.* The United States, No. H-210, now pending in the U. S. Court of Claims and which stands remanded to the general docket thereof to await the action of this Court herein; that the case in which he is counsel involves the construction and validity of the whole of Section 402 (*f*) of the Revenue Act of 1918, the language of which is identical with Section 402 (*f*)

of the Revenue Act of 1921; that counsel for both parties herein have consented in writing to the filing by the undersigned of a brief *amicus curiæ* and their consents have been filed with the clerk of this Court.

Wherefore, the undersigned prays leave to file herein and submit for consideration the within brief *amicus curiæ*.

Two questions have been certified by the Court of Claims. One of them is whether the tax imposed by the final clause of Section 402 (*f*) of the Revenue Act of 1921 on life insurance policies payable in terms to beneficiaries "other than the decedent or his estate" is a direct tax on property and void because not apportioned; and the other is whether the amount of tax imposed resulting from the inclusion in the gross estate of the insured bears such an unreasonable relation to the subject matter of the tax as to render it void. As to the first of these questions the query relates to life insurance policies payable to beneficiaries "other than the decedent or his estate." The import of the language "other than the decedent" seems obscure since no insurance can be payable to the decedent in any event, nor is insurance payable to the insured during his lifetime subject to the tax by any provision of the statute. It is assumed, therefore, that the Court of Claims intended the question to relate to insurance policies payable to beneficiaries other than *the executor* of the estate of the decedent.

The Statute Involved.

The statute is the Revenue Act of 1921 (42 Stat., 227), which in so far as it materially affects the questions at issue, provided as follows:

> "Sec. 400. That when used in this title—
>
> "The term 'executor' means the executor or administrator of the decedent, or, if there is no executor or administrator, any person in actual or constructive possession of any property of the decedent; • • •"
>
> "The term 'net estate,' means the net estate as determined under the provisions of Section 403;
>
> "Sec. 401. That in lieu of the tax imposed by Title IV of the Revenue Act of 1918, a tax equal to the sum of the following percentages of the value of the net estate (determined as provided in Sec. 403) is hereby *imposed upon the transfer of the net estate* of every decedent dying after the passage of this act, whether a resident or a nonresident of the United States: • • •"
>
> "Sec. 402. That the value of the gross estate of the decedent shall be determined by including the value *at the time of his death* of all property, real or personal, tangible or intangible, wherever situated—
>
> "*(a)* To the extent of the interest therein of the decedent *at the time of his death* which after his death is subject to the payment of the charges against his estate and the expenses of its administration and is subject to distribution as part of his estate:

> "(*f*) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life."

Section 403 provided for determination of the value of a statutory net estate by deducting various items and an exemption of $50,000 from the value of the gross estate. The tax is measured by certain percentages of this statutory net estate.

Section 408, as far as material, provided in part as follows:

> "If any part of the gross estate consists of proceeds of policies of insurance upon the life of the decedent receivable by a beneficiary other than the executor, the executor shall be entitled to recover from such beneficiary such portion of the total tax paid as the proceeds, in excess of $40,000, of such policies bear to the net estate. If there is more than one such beneficiary the executor shall be entitled to recover from such beneficiaries in the same ratio."

Section 409, so far as material, provided in part, as follows:

> "That unless the tax is sooner paid in full, it shall be a lien for 10 years upon the gross estate of the decedent, except that such part of the gross estate as is used for the payment of charges against the estate and expenses of its administration, allowed by any court having

jurisdiction thereof, shall be divested of such lien. * * *

"If insurance passes under a contract executed by the decedent in favor of a specific beneficiary, and if in either case the tax in respect thereto is not paid when due, then * * * the beneficiary shall be personally liable for such tax, and such property, to the extent of such beneficiaries' interest under such contract of insurance, shall be subject to a like lien equal to the amount of such tax."

Propositions of Law, and Argument.

There are raised several propositions of law which may be stated succinctly as follows:

I. The tax is imposed only on the transfer of the net estate of the decedent.

II. The amount receivable as insurance was not transferred by the decedent as a part of his net estate.

III. The tax is an excise upon the right to transmit and not upon the right to receive.

IV. The measure of the tax, in so far as it includes the insurance receivable, is unconstitutional.

Each of these four propositions of law will be severally discussed.

I. THE TAX IS IMPOSED ONLY ON THE TRANSFER OF THE NET ESTATE OF THE DECEDENT.

II. THE AMOUNT RECEIVABLE AS INSURANCE WAS NOT TRANSFERRED BY THE DECEDENT AS A PART OF HIS NET ESTATE.

It should be particularly noticed that the measure of the tax is on the value of a *statutory* net estate, which is the difference between the statutory gross estate defined in Sec. 402 and certain deductions therefrom set forth in Sec. 403. The tax is not imposed upon the transfer of the statutory gross estate. It is axiomatic that one must have owned a definite interest in property at or before the time of his death before he can be said to have transferred it by dying.

In respect of insurance, whether it be that receivable, after proof of the decedent's death, by his executors or by his widow, this decedent did not possess at any time during his life, nor did he have any right to, the amount of insurance receivable after his death. The only thing which he possessed at the time of his death or in which he had any right which he could possibly have been said to have transferred was the cash surrender value, if any, of the insurance policies. It would be necessary for the decedent to have surrendered such policies before dying in order that the cash value could be transferred by him as a part of his net estate. If he die without so surrendering them and collecting his interest therein, his right thereto lapses upon his death, and the thing which is receivable after his death is not the cash surrender value of these policies, but an amount the insurance company promised to pay because of his death, after due proof thereof. By entering into the contracts he could not

be said to have transferred property to take effect at or after his death, because he never owned at that time or at any time the amount which the insurance company promised to pay after his death by virtue of the contract.

It is scarcely necessary to state that a contract of insurance is regarded in law as a special contract, not subject to the rule regarding adequacy of consideration as are other contracts. If at the time of entering into these contracts decedent had paid to the insurance company a sum of money equal to the amount receivable as insurance after his death and in the contract the insurance company, in consideration of the payment of this amount, had promised and agreed to pay the decedent dividends or interest thereon during his lifetime and upon his death to pay the principal to his estate or to any designated person, then the amount receivable would be taxable, because it would be the equivalent of a trust created by him to take effect in possession or enjoyment at or after his death, of *property* which *he had placed in the trust*. Provision is made for taxing such a transfer in paragraph (*c*) of Sec. 402, but in contracting for insurance of this character known as "straight life insurance" one does not place property which he owns in trust. The insurance company does not agree to pay after his death any part of those premiums which he may have paid to the insurance company during his lifetime. It pays after his death something entirely different—something he never owned. But for the beneficent principle underlying insurance a contract of insurance would be

void as a wagering contract. As a matter of fact, to the extent of any insurance payable to one who has not an insurable interest in the life of the insured the contract is void except in a case where the policy is assigned to a creditor for a valuable consideration and only to that extent.

A marked difference between insurance contracts and other contracts is that before a contract can be one of insurance it must be based upon a risk. The maxim "If there be no risk there is no insurance" has always been used to determine the nature of the contract, for there is no consideration moving from the insured to the insurer at the time of the contract equal to the amount of the insurance provided for. Except for the risk involved, making the contract one of insurance, such contracts would ordinarily be subject to cancellation for inadequacy of consideration in any case where the insured failed to live long enough for the insurer to receive a fair consideration for his promise.

Life insurance contracts are not assurances for a single year with the privilege of renewal from year to year on payment of stipulated premiums, but are entirely contracts for life, subject to forfeiture by failure to perform the condition subsequent as to payment of an annual premium. (McMaster v. New York L. Ins. Co., 183 U. S., 25.)

Each policyholder in any insurance company, whether mutual or not, has an associated relation whereby he is interested in the engagements of all, as out of the co-existence of many risks arises the law of

average, which underlies all contracts of insurance. (New York L. Ins. Co. *v.* Statham, 93 U. S., 24.)

The fact that one may insure his own life but cannot assign the policy to another as a cover for a wager policy is the best proof that the engagement does not vest in him property, to the extent of the insurance contracted for, to be dealt with as he pleases (Aetna Life Ins. Co. *v.* France, 94 U. S., 561; Crotty *v.* Union Mutual Life Ins. Co., 144 U. S., 621).

In the case of Phœnix Mutual Life Ins. Co. *v.* Bailey, 13 Wall. 616, a policy of life insurance is defined to be not necessarily a contract merely of indemnity for pecuniary loss, as is that of marine and fire insurance, but it is sufficient if one has an insurable interest in the person insured at the inception of the contract and it has appeared that the stipulated event has happened which renders the insurance payable.

The amount receivable in insurance is much the same as the amount recoverable after one's death because of his death through the wrongful act of another. In such a case the only interest of decendent at the time of his death was the right to sue for injury done him by the wrongful act of another. If he failed to live until he should recover in the action, his suit upon his death would immediately abate, for his death ends any right he had. After his death his executor or administrator or his next of kin in some jurisdictions may maintain an action, not by reason of any interest or right which the decedent had at the time of his death or during his lifetime, but wholly by reason of his death, to recover indemnity therefor. As an illustra-

tion—one who is injured by the wrongful act of another in the District of Columbia can maintain a suit for any amount without limitation for the injury he has sustained. If he should die before recovering a judgment, the action abates. His executor or administrator only for his next of kin, who must be specifically named and shown to be his next of kin, may maintain a suit against the tort feasor, not for any injuries to decedent, but for causing the death of the decedent; and he is limited both in his action as well as in his right of recovery to $10,000, regardless of the loss sustained by the next of kin through the untimely death of the decedent. The thing, therefore, which his estate or his next of kin receives is nothing that the decedent transmitted as a part of his net estate, for it was not anything in which he had any right of property during his lifetime. No attempt has ever been made, nor could any be successfully made, to measure the transfer of one's net estate by including an amount so received after his death, which in its very nature is not the thing which the decedent ever possessed or had a right to during his lifetime. So it is with insurance. The thing receivable after death of the insured is not a thing which the decedent possessed or had any right to at any time during his life and which he could himself transfer.

Another striking illustration of a nontransferable interest arises where the decedent, during his lifetime, was the owner of a life estate in any property. Upon his death his estate or interest abates and he transmits from himself no interest in property to anyone else.

It is true that it requires his death before the remainderman may take the remainder, but the interest which the remainderman takes is not the interest which the life tenant had and transmitted from himself to the remainderman. The remainderman takes his interest by virtue of some antecedent authority. In the same way insurance receivable after decedent's death is not a thing which the decedent had and transmitted from himself by dying. As in the case of the life estate, it required the decedent's death before the beneficiary could get possession of the insurance, but the beneficiary acquires it through some antecedent authority. Neither in the case of insurance receivable nor estates in remainder does the ownership of property originate and come from either the insured or the life tenant. In the one case it arises by virtue of a contract and is payable wholly by an insurance company out of its own funds. In the other case the title springs from an original grant of some other person whereby the life tenant receives his particular estate created by someone else out of property which the life tenant did not own.

Article 12 of Regulations 37, revised 1919, relating to estate tax, promulgated by the Treasury Department under the Revenue Act of 1918, expresses clearly the kind of property upon which the taxe is imposed, as follows:

> "Article 12. Character of Interests Included. This provision is designed to include all property interests of the decedent, of whatever character. It is the commonest form of taxable

transfer. As a basis for tax, there must be an actual beneficial ownership in the decedent, not a bare legal title, or one held in trust. Thus, property actually devoted to religious or charitable purposes, and placed in the name of an individual solely for convenience in administration, is not included in his gross estate. The statute also includes only property rights *existing in the decedent in his lifetime and passing to his estate*. It consequently does not include a right which came into existence *only after the decedent's death*, such as a cause of action by statute for causing the death. The proceeds of such a cause of action should not be included in the gross estate, whether payable generally to the estate or to some specified class of persons, such as the widow or children.

"The value of a vested remainder should be included in the gross estate. Nothing should be included, however, on account of a contingent remainder where the contingency does not happen in the lifetime of the decedent, and the interest consequently lapses at his death. Nor should anything be included *on account of a life estate in the decedent*. There should be included, however, the value of an annuity payable to the decedent upon the life of a third person who survives him, and the value of an estate for the life of a person other than the decedent. For rules as to valuing such annuities and illustrations, see Article 20."

Attention is invited to the fact that the Revenue Acts of 1921, 1924 and 1926, following the Revenue Act here under consideration, differs therefrom in the lan-

guage used in imposing the tax. The 1918 Act imposes the tax upon the transfer of the actual net estate of the decedent and measures it by a statutory net estate. The subsequent acts impose the tax upon the *statutory* net estate and measure it by the *statutory* net estate. This has been accomplished in a way not easily discernible, thus: The language of Section 401 of the 1918 Act, which imposes the tax, is not different from the language of the same sections of the subsequent acts which impose the tax; but in the subsequent acts it will be found that there has been inserted, in the section *defining terms used*, that the term "net estate" means the statutory net estate. This will be found in Section 400 of the 1921 Act, in Section 300 of the 1924 Act, and in Section 300 of the 1926 Act, but it will not be found in Section 400 of the 1918 Act.

III. The Tax is an Excise upon the Right to Transmit and not upon the Right to Receive.

The tax imposed by this act is not based upon any legacy or thing that any person receives, whether he be as individual or *nominee* or the executor or administrator, but is based solely upon the right of an individual to transmit from himself an interest in property by the act of dying. On the other hand, a legacy or an inheritance tax is in terms based upon the receipt by anyone of an interest in property passing to him either by the will of a person who has died, or inherited by or distributed to him by virtue of the intestate laws of the State.

In the case of Fidelity Trust Company *v.* McCaughn, held that the estate tax imposed by the Revenue Act of 1918 is not a tax on succession and receipt of benefits under the intestate law or a will, but is an excise on the transfer of an estate on the death of the owner.

In the case of Fidelity Trust Company *v.* McCaughn, 17 Fed. (2d), 605, it is held that the word "interest" used in Section 402 of the Revenue Act of 1918, for the purpose of determining the tax by virtue of the passing of the decedent's property, means the use of the *physical thing* as well as an *estate therein.*

A clear distinction between estate and inheritance taxes is set forth in the case of Frick *v.* Lewellyn, 298 Fed., 803.

To the same effect is the case of Frew *v.* Bowers, 12 Fed. (2d), 625, which holds that the estate tax under the 1921 Act is an excise on the right or privilege of transmitting property from a decedent and not on the right or privilege of receiving it.

But the tax in this case is based solely upon the right of a person dying to transmit property, and the insurance which was receivable in this case was receivable only by virtue of *a contract* which imposed a liability upon *an insurance company* which had assumed the risk on this decedent's life. Such insurance, therefore, to the extent of the amount receivable, either by the executor or by a widow, is not transferred by a decedent as a part of his net estate. We often hear it said that a man left little or no estate but left considerable insurance.

Subsequent to the passage of the 1921 Act, the Treasury Department issued Regulations 63, under the Revenue Act of 1921, and in Article 1 thereof it has placed its executive construction upon the meaning of Section 401 of the said act as follows:

> "Article 3. Neither a Property nor a Legacy Tax.—The Federal estate tax is imposed upon the transfer of the net estate, determined in the manner prescribed, of every person dying after September 8, 1916. The tax is not laid upon the property, but upon its transfer *from the decedent* to others. The subject of tax is the transfer of the entire net estate, not any particular legacy, devise, or distributive share. It is not an individual inheritance tax. The value of the separate interests and the relationship of the beneficiary to the decedent have no bearing upon the question of liability or the extent thereof. The transfer of property is taxable, although it escheats to the State for lack of heirs."

It will be seen that the Department's own construction of this act is that it contemplates a tax upon the transfer of property from the decedent to others and that it bears no relation to an individual inheritance tax. Is the amount of insurance receivable after decedent's death under contracts of insurance over property which the decedent owned and which he transferred? It cannot be, for he not only never owned such amount, but the contracts specifically provided that he should never own it.

IV. The Measure of the Tax in so far as it Includes the Insurance Receivable is Unconstitutional.

At the outset it should be borne in mind that to whom the insurance company pays the amount of insurance is wholly immaterial, since Section 401 imposing the tax admittedly bases it, not upon the receipt of property, but upon its transmission by the decedent at the time of his death. The fact that the insurance may be payable to the executor does not render the amount so paid any more the property of the decedent at the time of his death than if the amount were paid to some member of his family not his executor; otherwise it would be a tax on the right to receive and not on the right to transmit.

Obviously one takes out insurance, not in order to enrich himself and thus acquire property, but quite the reverse because he may not have property to transmit. In order to impose a tax supposed to be upon the transfer of the net estate it is proposed to measure the tax not only by the transfer of the only property one is capable of transferring, but by adding thereto that which he never had and never could have had and therefore never transferred. It is included only, as the statute says, because it is *receivable* by some one after his death, by virtue of a contract entered into in his lifetime. The statute makes no pretense of including it in the gross estate as a *transfer* by him.

We concede that Congress has the constitutional power to impose an excise upon the event of the taking

out of an insurance policy measuring the tax by the amount of the insurance. Likewise we concede authority to impose an excise on an insurance company based upon the event of issuing a policy of life insurance to be measured by the amount of the insurance.

It may be lawful also to impose an indirect tax upon the right to receive proceeds of an insurance policy regardless of who was the insured, the tax to be payable by the beneficiary and measured by the amount of insurance. But the tax here involved is (*a*) upon the right of a person dying to transmit his property to the living (Sec. 401); and it is at the same time a tax upon one who receives insurance (Secs. 408-409). While a separate excise on insurance received, measured by the amount thereof plus any other property the *recipient* may happen to have at that time might operate uniformly, it would be extremely arbitrary, if not a direct tax on the other property. But an excise upon the event of receiving insurance measured by the amount thereof plus the amount of property *some one else* may happen to have possessed at death, and, by dying, transmitted to another, or others, is arbitrary beyond the realms of reason, if not a direct tax on the other property.

I doubt seriously if Section 402 (*f*) would operate with the geographic uniformity contemplated by the Constitution in respect of the levying of indirect taxes. Suppose "A" took out a policy of insurance in the amount of $100,000, which, after his death, was receivable by his widow and that at the time of his death he had no property and transmitted no net estate.

Under the statute $60,000 of this insurance would be included in his gross estate and as there is an exemption of $50,000 there would be a tax on the $10,000 remainder payable in its entirety by his widow as the decedent had no property. Suppose "B" at the same time took out a similar insurance policy and after his death his widow received $100,000 and that "B" left no property at his death but owed debts in the amount of $10,000. $60,000 of the insurance would be included in his gross estate but after deducting his indebtedness of $10,000 and the specific exemption of $50,000 his estate would not be taxable and his widow would pay no tax, nor would she have to pay any of the debts. In the one case a tax is imposed upon one widow where a man transmitted no property by dying and no tax would be paid by the other widow where her deceased husband transmitted no property by dying, and in each case the widow received the same amount of insurance.

As a matter of fact, under the provisions of this act if a man should die possessed of no property, but sometime before his death had taken out insurance for the benefit of his family, his estate as well as the beneficiaries of the insurance would be liable for the full amount of this tax although the insured transmitted no net estate when he died and although the beneficiary of the insurance received the amount of the insurance not by virtue of any transfer from the decedent, but by virtue of some antecedent authority.

It must be conceded that generally speaking one takes out ordinary insurance not for his benefit but for the protection of those dependent upon him because

he may not have any or a sufficient net estate to transmit to them when he dies. Even though one may possess considerable property he may still contract for insurance for the benefit of his dependents, for he is subject to be sued for damages; or he may lose in investments; or his property may be stolen or destroyed, and thus that which belonged to him may be wiped out some day so that he could not transmit a net estate.

To extend the argument logically, the provisions of this act are tantamount to the imposition of a tax upon the transfer of a man's net estate measured by the value not only of his net estate, but that plus the value of any property which the recipients of his net estate may happen to possess in their own right at the time of his death.

In the celebrated case of Knowlton *v.* Moore, 178 U. S. 41, *47*, the Supreme Court says:

> "Direct taxes bear immediately upon persons, upon the possession or enjoyment of rights, indirect taxes are levied upon the happening of an event or an exchange."

The event, the generating source creating the right to receive insurance, happens at the time the contract therefor is entered into. The presentation of due proof of death of the insured may be the event required to happen before the beneficiary may gain possession of the insurance, but neither that event nor the event of the insured dying and transmitting a net estate is the generating source or the event by which the insurance is created or transmitted. As heretofore shown,

one may have a life estate in property and it may require his death before the remainderman may actually receive his estate in remainder, but the generating source of the remainder is not the event of the life tenant dying and transmitting a net estate, but it is the deed which created the title in the remainderman.

Contracts of insurance are not subject to any direct or indirect tax when they are taken out. That the insured subsequently dies and at that time happened to transmit a net estate having nothing whatever to do with the contract of insurance, does not furnish authority retrospectively to impose a tax upon this past event payable by some one other than the contracting parties and measured not alone by the amount of the insurance, but by the amount of property which the insured happened to have possessed at the time of his death.

In short, if this tax is good as an indirect tax upon the insurance, it is necessarily a direct tax on the other property by which it is measured; and conversely, if this tax is good as an indirect tax on the transfer of the decedent's net estate, it is a direct tax on the amount of insurance by which it is measured.

Respectfully submitted,

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